



# Implementing Client Protection in Microfinance

The State of the Practice, 2011



Keeping clients first  
in microfinance



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The State of the Practice, 2011

A Report from the Smart Campaign

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## Preface

Recognizing a need to make the commitment to client well-being explicit and actionable, the providers, investors, donors, and support organizations that make up the microfinance community introduced the Client Protection Principles (CPPs) in 2008. The Smart Campaign was launched in 2009 to assist the microfinance industry in implementing the principles. The Campaign now has over 2,300 endorsers from 130 countries, including 700 microfinance institutions (MFIs).

After nearly two years, it is possible to begin to take stock of the Smart Campaign and, more broadly, of the state of client protection in microfinance. This mid-term report from the Smart Campaign has two main purposes. The first is to explain how the Smart Campaign and actors throughout the microfinance industry are working to move from initial awareness raising about client protection to capacity building, implementation, and finally certification. The second and possibly more important purpose is to provide a first look at how the microfinance industry is doing on the CPPs. That look is gleaned from the on-site assessments of CPP implementation at over 300 financial institutions. The assessments were performed by rating agencies, investors, and the Smart Campaign during the period 2008–2011. This is by far the most comprehensive data yet assembled on client protection practices at microfinance institutions, though it is a first cut. We expect the consistency and coverage of the dataset to improve significantly in future reviews.

The early news is heartening. The vast majority (88 percent) of all the financial institutions received passing marks, and these results also held for the two all-important principles, avoiding over-indebtedness and transparency. Given the nascent state of the Smart Campaign during the period when the assessments were performed, the scores cannot be attributed entirely to the Campaign. Rather, they reflect the rapid coming together of the microfinance industry around the CPPs, as demonstrated by the raters and investors that incorporated the CPPs into their assessments and the MFIs that sought to be assessed. The results show that a basic level of client protection performance is widespread in the practices of many MFIs.

Of course, the industry has significant room for improvement, and will continue to face critical challenges that it must respond to in the face of changing competitive conditions. This report provides some confidence that the microfinance industry has a positive base of pro-client practices to build on as it seeks to fully implement its commitment to client protection.

Isabelle Barrès  
Smart Campaign Director

## Acknowledgments

This report would not have been possible without the organizations that have shared their data and experiences with assessing and implementing client protection. A special thanks goes to the microfinance rating agencies MicroFinanza Rating and Planet Rating, and the investment managers BlueOrchard, Incofin, Symbiotics, and Triple Jump, whose data form the basis for this report. For most of these institutions, this is the first time they have been asked to share their client protection data, and we recognize them for their willingness to do so. Thanks also to responsAbility and Oikocredit for providing input on their client protection activities.

Thanks also to the leaders of the microfinance institutions who shared their experiences with implementing client protection: AccessBank (Azerbaijan), Arohan (India), FMM Popayan (Colombia), Fonkoze (Haiti), and Ujjivan (India), as well as *MFTransparency* for sharing its case study on Gatsby Microfinance.

This report was prepared by the Smart Campaign staff at the Center for Financial Inclusion at ACCION. Charlotte Connors directed the project, and Daniel Rozas was the lead analyst and author, with assistance from intern Laura Galindo, whose support far exceeded the title of her position. Substantial input was also received from Isabelle Barrès and Elisabeth Rhyne, with additional input from Sergio Guzmán. Thanks also to Smart Campaign Steering Committee members Ben Simmes, Beth Porter, Dave Grace, and Kate McKee, who provided thoughtful feedback on this report.

In addition to providing data, the following rating agency and investment manager representatives also provided valuable and substantial input: Emmanuelle Javoy (Planet Rating), Lucia Spaggiari and Micol Guarneri (MicroFinanza Rating), and Ximena Escobar de Nogales (BlueOrchard).

The Smart Campaign would like to recognize the contributions of its sponsors – ACCION International, Credit Suisse, Deutsche Bank, Ford Foundation, the International Finance Corporation (IFC), the MasterCard Foundation, the Small Industries Development Bank of India (SIDBI), and the U.S. Agency for International Development (USAID) who have made it possible for the Smart Campaign to reach out widely across the microfinance industry.



## **Part I. The Smart Campaign and the Practice of Client Protection in Microfinance**

### **Why Client Protection? Why Now?**

Much of microfinance is socially motivated. The goals may be varied: to help individuals and families save for the future, pay for school for their children, build small businesses, cope with unexpected setbacks such as illness or poor crops, or simply provide access to financial services that others take for granted. But before any of these goals can be met consistently, microfinance institutions must first meet another objective: that the services they provide meet minimum standards of quality.

Client protection covers many dimensions of product and delivery quality, from ensuring that microcredit products will not result in further impoverishment of already poor clients to providing reliable channels for addressing client complaints. But at heart, client protection is built on a notion that is self-evident: that clients be treated with transparency, respect, and prudence. This is especially important for the vulnerable, low-income populations that make up the bulk of microfinance clients. It is a must for new clients who lack experience – those in newly penetrated areas and young people. It is critical for clients who are served by institutions that operate in environments of limited government regulation.

Financial service providers have power and information advantages over such clients that create the opportunity – or even temptation – for abuse. To ensure that such abuse does not take place, providers must implement strong client protections and enforce them with continual vigilance.

In the past, microfinance institutions may have taken client protection for granted, but the events of the past few years demonstrated a need for more explicit attention. In the mainstream financial sector, the subprime mortgage debacle raised general public awareness about such issues. In microfinance, awareness began to rise with the industry-wide debate over microfinance interest rates following the IPO of Compartamos in 2007. While microfinance interest rates are necessarily relatively high, questions were – and will always be – raised about charging the poor more to borrow than the rich. Clients of microfinance institutions (MFIs), regulators, investors, and the public need confidence that MFIs charge transparent and responsible prices.

Attention was further drawn to client protection as a result of the problem of over-indebtedness in several countries, where it arose precisely because microfinance there was successful and growing rapidly, leading to market saturation and multiple providers competing for the same clients. As more markets become competitive, providers need to practice restraint, particularly since, as behavioral research demonstrates, many people have a propensity to overestimate their own capacity for debt. In some of the markets where over-indebtedness appeared, charges of harsh collections practices also surfaced, drawing attention to the need for respectful face-to-face treatment of clients.

These experiences have focused attention on the importance of ensuring that sound client protection practices are in place. There is no controversy that protecting clients is the right thing to do – after all, that is how each of us would wish our own financial services providers to behave. But protecting clients also happens to be the smart thing for the industry to do. The Smart Campaign argues that financial institutions that protect clients will create a responsible and loyal clientele, while protecting themselves from the reputation risk that can come with bad practices.

### **The Client Protection Principles and the Smart Campaign**

When the Smart Campaign was publicly launched in October 2009, it took on a major challenge: to embed the Client Protection Principles (CPPs) deep within the institutional culture of the microfinance industry. Since then, the Campaign has made enormous strides toward that end. The microfinance industry has embraced the

CPPs and the Campaign. It has mobilized itself in numerous ways to make client protection integral to the industry's common goals. To date, the Campaign has garnered more than 2,300 endorsements from over 130 countries, including approximately 700 MFIs; 130 investors and donors; 250 networks, associations, and other supporting organizations; and 1,200 individuals.

Because the CPPs embody views that are widely shared among industry participants, it was relatively straightforward for the microfinance community to agree in mid-2008 on the basic norms that make up the Client Protection Principles.<sup>1</sup> However, even as they signed on to the CPPs and joined the Campaign, endorsers asked one question over and over: How can we put these principles into practice?

Since it officially began in October 2009, the Smart Campaign has focused on answering that question by creating and disseminating tools and training, engaging with all corners of the microfinance industry, and observing practices on the ground through on-site assessments. National and regional microfinance associations from 30 countries have joined the Campaign in formal relationships, resulting in the training of 53 trainers and 42 assessors who are active in spreading know-how on client protection to nearly 1,000 managers and staff of MFIs. Client protection and responsible finance have been (and continue to be) topics at every major microfinance conference worldwide. Overall, the Campaign can already claim to touch organizations that serve more than 40 million low-income people. All this in less than two years.

At this point, just beyond the halfway mark of the Campaign's original three-year life span, it is important to begin to ask whether this flurry of activity is actually making a difference in the operations and day-to-day practices of providers. This report, commissioned by the Smart Campaign's Steering Committee (see Appendix I for a list of members), is a first stocktaking of the state of the practice among providers.

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1. The CPPs drew on codes of conduct that had been adopted several years before by a number of organizations, including the SEEP Network, the Microfinance Network, ACCION, Freedom from Hunger, and others.

The first section of this report provides an update on the activities that the Campaign has undertaken. It recaps the Campaign's efforts to date, from endorsement to tool development to implementation, along with continuing focus on building awareness. The second and third sections of the report examine how MFIs are implementing the CPPs, using a dataset that combines third-party assessment information from a number of rating agencies, investors, and the Campaign itself. This is supplemented by short case studies, each explaining how a provider has implemented a specific principle. The report provides a first systematic look at the actual client protection practices of MFIs across the world, something that has not been done before. The final section of the report discusses the next steps for the Campaign, including the introduction of a client protection certification process for providers.

## **The Smart Campaign's Major Activities to Date**

### **From Awareness to Understanding**

The Campaign began by conducting a strong outreach effort to deepen industry understanding of the CPPs. More than 30 national-level associations (see Appendix II for a list) around the globe have formed partnerships with the Campaign to communicate with their members about the CPPs, as well as the resources the MFIs have available to implement client protection. To facilitate the spread of actionable information, the Campaign has provided comprehensive training to the staff of all of partner associations, to help them assess the practices of their members and communicate about national and regional client protection issues. The Campaign further supports these efforts by reaching out across the language barrier. Its website and many of its tools are available in five languages: English, Spanish, French, Russian, and Arabic.

The Smart Campaign works with major players in microfinance who are also committed to making client protection an integral part of the industry. CGAP, one of the industry's leading knowledge institutions and a founding partner of the Campaign, has provided a steady stream of focus notes, blog posts, and technical tools on client protection. In September

2009, CGAP published the first edition of a technical guide for investors to support the integration of the CPPs into investors' policies and processes, which was updated in 2010. The SEEP Network, another early Campaign partner, paved the way for the Campaign's formal partnerships with regional and national associations, by contributing their expertise and leveraging their relationships.

In addition, the Campaign collaborates closely with *MFTransparency*, which provides for guidance on pricing transparency, one of the CPPs. It also works closely with the Social Performance Task Force (SPTF), which helps integrate the CPPs into a broader framework of social performance management and reporting for the microfinance industry. Other Campaign collaborators include MIX Market, Mission CRS, UNDP, and Terrafina Microfinance.

One special source of support for the Campaign's agenda has come from a group of microfinance rating agencies that conduct MFI social performance ratings, which include assessments of client protection practices. The field experience of the rating agencies in evaluating MFI practices has proved an invaluable resource to the Campaign when developing its own Client Protection Assessment methodology. These rating agencies have also helped deepen the Campaign's impact by aligning their pre-existing client protection evaluation frameworks with the CPPs.

Finally, the Campaign has also been working closely with the microfinance investor community, especially with the managers of microfinance investment vehicles (MIVs). As part of their evaluation of poten-

tial investee MFIs, as well as ongoing monitoring of existing portfolio investments, many funds conduct on-site due diligence evaluations. The Campaign has collaborated closely with these investment managers to help integrate evaluation of the CPPs into their due diligence process. The success of this project has demonstrated the level of investor interest in client protection – as during the past year alone, at least 10 major microfinance investment funds managing over US\$2 billion have integrated client protection into their due diligence and reporting.

### Building a Toolbox

Building awareness was a two-way street for the Campaign. While it was busy educating the industry on client protection, the Campaign was simultaneously in listening mode. As the Campaign initiated conversations across the industry, through email, conferences, webinars, and focus groups to learn what was needed to make client protection a reality, one of the most common responses was: Give us tools.

The Campaign became a virtual workshop. Or rather, an assembly shop. Some tools were built based on the methodology developed in “Beyond Codes,” an action research project of the Center for Financial Inclusion at ACCION documenting the experiences of leading institutions. The Campaign also recognized the wealth of resources that were already in use at MFIs, though not necessarily widely known or shared. Through its “call for tools” the Campaign invited MFIs, investors, donors, and professional trade associations to contribute their own policies, codes of conduct, and training materials on client

#### Box 1. An Investor Investing in Client Protection

Microfinance investors play a special role in setting the tone for the uptake of client protection at their portfolio institutions. One such example is Oikocredit, which became an early endorser of the Smart Campaign and promptly encouraged its 500+ partners to follow suit. More than 220 Oikocredit partners (44 percent) have since endorsed the Campaign, halfway to the goal of 80 percent endorsement by the end of 2012. Oikocredit has modified its due diligence process to weigh client protection more heavily: It now makes up 40 percent of the overall score. This year, Oikocredit has sponsored workshops, conferences, and trainings for many of its investees, to educate them about the CPPs. It trained all of its own officers in India and coordinated CPP trainings in the Philippines, Kenya, and Cambodia, with more to follow through the rest of the year.

In September 2011, Oikocredit staff directly participated in the Smart Assessment of one partner MFI, Janalakshmi Financial Services Private Ltd in India. Going forward, Oikocredit plans to invite Janalakshmi staff to be part of a new core of trainers who share best practices with their peers, thereby facilitating the spread of client protection know-how across the region.

protection, enlarging the Campaign's library of resources.

The Campaign's process of learning, assembling, recycling, and developing new tools resulted in a suite of nearly 50 tools that are helping MFIs to move from endorsement to implementation of the Client Protection Principles. The tools provide MFIs with concrete examples of how their peers put the principles into practice, along with how-to guides for assessing and implementing best practices. The Campaign also developed a place to house all the resources it accumulates. In March 2010, the Campaign launched its website, [www.smartcampaign.org](http://www.smartcampaign.org), as the virtual headquarters of the Campaign and the "go-to" resource for client protection content for the microfinance industry. Since then, the site's tool pages have logged more than 81,000 visits (see Appendix III for a list of the top 15 tools viewed).

The tools continue to be improved and expanded. The Campaign encourages feedback from users on the existing tools, so that staff can address any perceived shortcomings and make needed modifications. Simultaneously, the Campaign has been shifting emphasis to supporting the use and implementation of these tools, including through targeted training curriculums. To date, the Campaign has trained 415 MFIs (nearly 1,000 MFI staff), with the goal of enabling them to conduct the Smart Campaign Self-Assessment ("Getting Started Questionnaire"). To date, 98 MFIs have submitted self-assessments to the Campaign as a first step toward improving practice.

In a bigger step, 26 MFIs have commissioned in-depth client protection assessments by the Smart Campaign (see Appendix IV for a list of Smart Assessed MFIs). The Smart Assessment is a diagnostic tool for microfinance institutions that helps them thoroughly examine implementation of client protection practices with the assistance of an independent third party. It is a mechanism for mitigating risk, taking the MFI through a process of internal review

to identify strengths, weaknesses, and ultimately opportunities to enhance business practice with a double bottom line. Through these assessments, the Smart Campaign has also deepened its knowledge base about client protection, identified best practices (written up in several of the case studies below), and initiated a number of innovative pilot projects to improve areas where weaknesses have been identified.

### Evolution of the Principles

Beginning in late 2010, the Smart Campaign's Evolution of the Principles Task Force, made up of representatives from MFIs, investors, and support organizations, initiated an in-depth examination of the existing CPPs (see Appendix V for a list of all the Smart Campaign's task forces and their members). The task force recognized that in their initial form the principles focused strongly on credit, and did not address the full range of financial services. In addition, the task force felt that it was important to include the concept of "nondiscrimination" in the principles, noting that MFIs should avoid discrimination in client selection and treatment on the basis of gender, ethnic origin, religion, or disability. The resulting revisions also included some realignment of the original principles.

The Smart Campaign's Steering Committee shared the proposed revisions with the microfinance industry for public comment in March and April 2011. Practitioners, investors, networks, donors, supporting organizations, and consultants from around the world wrote to express their views. The comments were thoughtful and highly supportive of the changes. They emphasized the importance of keeping the principles aligned with the issues relevant to microfinance, particularly the prevention of over-indebtedness. The task force consolidated the feedback and with Steering Committee approval in June 2011, the revised principles became official (see Box 2).<sup>2</sup>

2. Due to the recent change, the data sources in this report are largely based on the principles in their original form.

## Box 2. The Client Protection Principles (adopted in June 2011)

### **Appropriate product design and delivery**

Providers will take adequate care to design products and delivery channels in such a way that they do not cause clients harm. Products and delivery channels will be designed with client characteristics taken into account.

### **Prevention of over-indebtedness**

Providers will take adequate care in all phases of their credit process to determine that clients have the capacity to repay without becoming over-indebted. In addition, providers will implement and monitor internal systems that support prevention of over-indebtedness and will foster efforts to improve market level credit risk management (such as credit information sharing).

### **Transparency**

Providers will communicate clear, sufficient and timely information in a manner and language clients can understand so that clients can make informed decisions. The need for transparent information on pricing, terms and conditions of products is highlighted.

### **Responsible pricing**

Pricing, terms and conditions will be set in a way that is affordable to clients while allowing for financial institutions to be sustainable. Providers will strive to provide positive real returns on deposits.

### **Fair and respectful treatment of clients**

Financial service providers and their agents will treat their clients fairly and respectfully. They will not discriminate. Providers will ensure adequate safeguards to detect and correct corruption as well as aggressive or abusive treatment by their staff and agents, particularly during the loan sales and debt collection processes.

### **Privacy of client data**

The privacy of individual client data will be respected in accordance with the laws and regulations of individual jurisdictions. Such data will only be used for the purposes specified at the time the information is collected or as permitted by law, unless otherwise agreed with the client.

### **Mechanisms for complaint resolution**

Providers will have in place timely and responsive mechanisms for complaints and problem resolution for their clients and will use these mechanisms both to resolve individual problems and to improve their products and services.

More detailed guidance about the CPPs may be found on the Smart Campaign website under Client Protection Principles.



## Part II. Gathering Reliable Information on Client Protection Practices

The central aim of this section and the next is to gather and present what is known about the state of MFI implementation of the Client Protection Principles around the world. To our knowledge, this represents the first time that an effort has been made to evaluate existing client protection practices in microfinance on a global level.

To a large degree, such an effort a year or more ago would have faced a substantial dearth of information. It is thus a testament to how rapidly the notion of client protection has gained acceptance that there is now a substantial body of data in the form of individual social performance ratings by professional rating agencies, social due diligence and reporting by MIV managers, client protection reports on MIX, and data gathered by the Smart Campaign itself.

This report draws on three main types of data. The first type is a set of **specific examples** of client protection practices of MFIs around the world. These mini case studies, interspersed in boxes throughout the paper, are sourced mainly from Smart Campaign assessments, particularly examples where organizations decided to make changes based on findings during the assessment process. The Campaign conducted follow-up interviews to document the progress and detail of the initiatives.

The second type involves two streams of **self-reported data** submitted by MFIs:

*MIX Social Performance Reports.* The client protection portion of the MIX social performance report is a shortened form of the Smart Campaign’s “Getting Started Questionnaire.” The advantages of these data are that it is easy to synchronize with other Smart Campaign data sources because it tracks all the Client Protection Principles and a significant number of MFIs have filled it out (350 in the latest year available on the MIX, 2009). The disadvantages, however, are that it is relatively superficial and self-reported.

*The Smart Campaign’s “Getting Started Questionnaire.”* This 42-question checklist helps MFIs assess their own practices as a way to identify areas they may wish to improve. To

date the Campaign has gathered 98 “Getting Started Questionnaires” through its work with regional and national microfinance associations. These data are more detailed than the MIX reporting, but are also self-reported.

Self-reported data are indicative, but not reliable. They show that many MFIs around the world have taken the next step beyond endorsing the Campaign on the path toward implementation. At a minimum, they suggest that these organizations have more than casual awareness of client protection and are to some extent evaluating their practices.

However, self-assessments are likely to be biased, as MFI managers generally rate their own performance better than do third-party observers. This trend is especially evident in those client protection areas that tend to have broader awareness, such as prevention of over-indebtedness and transparency (see Table 1).<sup>3</sup> It is possible that categories that receive less attention, such as mechanisms for complaint resolution and privacy of client data, are graded more critically by MFIs because they are less well understood or seen as less important.<sup>4</sup>

To minimize the effects of bias, the remainder of this report uses self-reported data sources only sparingly and excludes them from the main dataset that forms the core of the analysis in this and the next section.

Instead, the report relies extensively on a third source of **third-party assessment data**, the **CPP Benchmarks 0.1**. This dataset was constituted specifically for this paper, and comprises third-party on-site evaluations drawn from multiple sources: ratings by the specialized microfinance rating agencies MicroFianza Rating and PlanetRating; due diligence evaluations by the asset managers BlueOrchard, Incofin,

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3. For CPP Benchmarks, grades for Privacy of Client Data, should not be compared with other categories, given data limitations and significant deviations from the norm.

4. The binary social performance reporting to MIX, which requires a “Yes” or “No” for broad questions, results in exaggerated scores, and may skew negative when respondents are unfamiliar with the types of practices that underlie some of these categories. By the same token, they may skew positive when respondents are aware of something their MFI may be doing in a particular category, even if it may be of minor significance.

**Table 1. Scoring, Third-Party vs. Self-Assessments**

	PREVENTING OVER-INDEBT.	TRANS- PARENCY	RESPONSBL. PRICING	APPROPR. COLLECTIONS	STAFF ETHICS	COMPLAINT RESOLUTION	PRIVACY OF DATA
CPP Benchmarks (N=30)*	4.1	4.2	3.0	3.7	3.6	4.0	4.3
Self-Assessment Questnr. (N=30)	4.5	4.4	4.5	4.0	3.9	3.6	3.8
CPP Benchmarks (N=49)**	4.2	4.3	3.6	3.8	4.3	3.9	4.5
MIX (N=49)	4.4	4.8	3.7	n/a	3.4	3.2	3.4

\* Comparison between the Smart Campaign “Getting Started Questionnaire” (self-reported) and CPP Benchmarks (third-party); same MFIs.

\*\* Comparison between MIX Social Performance Data (self-reported) and CPP Benchmarks; same MFIs.

Symbiotics, and Triple Jump;<sup>5</sup> and assessments conducted by the Smart Campaign itself.<sup>6</sup>

In all, the CPP Benchmarks 0.1 include 479 independent third-party ratings or evaluations, covering approximately 300 MFIs – an unprecedented compilation of independent evaluations of client protection practices in microfinance (see Tables 2 and 3). Given the relative numbers of evaluations, the compiled dataset strongly reflects investor evaluations, which are less intensive and systematic than either rating agency assessments or Smart Campaign assessments. They are also less closely calibrated to the CPPs. This should be kept in mind when examining the results.

Creating the CPP Benchmarks 0.1 was as much an exploratory effort as it was a data-gathering one. The path taken for this research involved requesting contributors to provide their client protection data in the original format. The result is the most complete set of data we could gather, but it also meant that comparisons were not necessarily easy to make.

Each source varied in both depth and type of coverage. The Smart Campaign carries out in-depth assessments organized around the CPPs. Rating agencies have increased the depth and coverage of client protection to include detailed assessment of each

client protection principle, though without necessarily giving each principle its own separate grade.<sup>7</sup> Investors are the least likely to cover the CPPs in a systematic form, including some principles but often excluding others. All these evaluations were also conducted following different templates and carried out by assessors who had received different levels and types of training.

Although the quality of all these evaluations is varied, they are nevertheless a significant improvement over self-reported data. With combined evaluations providing at least 100 observations for each principle (see Figure 1), the resulting dataset is also large enough to support some level of exploration. By combining the Benchmarks with data available on MIX, we were able to enhance the view with other institutional variables, including institution type, size, geographic region, as well as financial indicators that enable an enhanced perspective of these financial institutions.

Finally, it is worth noting that each contributor also used its own unique scaling, which had to be rescaled to a standard format that could be compared across. For this we chose the Smart Campaign methodology that scores client protection practices on a scale of 1 (weak) to 5 (excellent). For a more detailed description of the methodology behind CPP Benchmarks 0.1, please refer to Appendix VI.

Besides revealing valuable information about the MFIs, the Benchmarks also tell us something

5. In addition, responsAbility shared its assessment methodology, and this has been included when evaluating the level of investor coverage of each principle.

6. For more on Smart Campaign assessments, see <http://www.smartcampaign.org/assessment>.

7. However, each principle is covered in the narrative report.

**Table 2. Data Sources for Client Protection Practices**

	DESCRIPTION	YEARS COVERED	NO. OF OBSERVATIONS	NO. OF MFIS	SCALE	LEVEL OF DETAIL	EVALUATION
Self-Reported Data	7 CPP categories; varied frameworks	2008–11	429	375–400	Various	Various	self
MIX Social Performance	6 CPP categories; 1–2 indicators per category	2008–09	350	350	0 or 1	Low	self
Smart Cmpgn Getting Started Questnr.	7 CPP categories; multiple indicators per category	2009–11	79	75	1–5	High	self
CPP Benchmarks 0.1	7 CPP categories; compiled from multiple sources	2007–11	479	275–325	rescaled to 1–5	Various	3rd party
Rating Agency Ratings	PlanetRating, MicroFinanza Ratings, both based on field visits	2007–11	110	100	Various	High	3rd party
Investor Due Diligence	Blue Orchard, Incofin, Symbiotics, Triple Jump; various methodologies, all include field verification	2007–11	357	200–250	Various	Low/ Moderate	3rd party
Smart Campaign Assessments	7 CPP categories; based on field visit assessments	2009–11	12	12	1–5	High	3rd party

about the evaluators themselves. The rating agencies provided grades either on a per-principle basis, or a composite grade, reflecting multiple principles. However, this was not the case with investors, whose reports clearly demonstrate that the principles are not equal in perceived importance. Thus, the two most prominent principles, prevention of over-indebtedness and transparency, are included in all investor evaluations. Meanwhile, appropriate collection practices and privacy of client data are often omitted. Indeed, only one of the five polled investment managers evaluated privacy of client data in its due diligence.

**Table 3. Sources for CPP Benchmarks**

SOURCE TYPE	# OF EVALUATIONS	OVERALL SCORE
MIV	357	3.9
Rating Agency	110	3.3
Smart Campaign	12	3.5
<b>Total</b>	<b>479</b>	<b>3.8</b>

Source: CPP Benchmarks 0.1.

The level of detail devoted to each principle suggests a similar pattern. Thus, while investment managers evaluated prevention of over-indebtedness and transparency on the basis of an average of three indicators, most of the remaining principles were evaluated on just one indicator, if at all.

### First Benchmarks on Client Protection Practices

The scores from the CPP Benchmark 0.1 dataset should be seen as a first indication of industry-wide performance. As a first attempt to pull together disparate sources of information on client protection that were not necessarily developed with similar standards and purposes, the dataset can be considered a beta version of what could become a more solid compilation with useable benchmarks in the future. However, it is important to keep in mind that, because of the aforementioned differences in underlying scales and evaluation frameworks, strict comparisons should be avoided, though general trends can be observed.

Most MFIs' client protection practices score adequate or above, and the distribution is heavily posi-



**Figure 1. Number of MFIs Evaluated for Each Principle**



tive, with 87.6 percent of MFIs receiving at least adequate marks (3.0 or higher) in overall client protection (Figure 2). However, there are a number of factors that cause these scores to be higher than the equivalent Smart Campaign Assessment grade would be (see Appendix VI). **The resulting positive evaluation level should thus be viewed with a degree of skepticism.**

However, the scores can be used to evaluate differences between groups of MFIs. Thus, while most regions show relatively little differentiation on over-

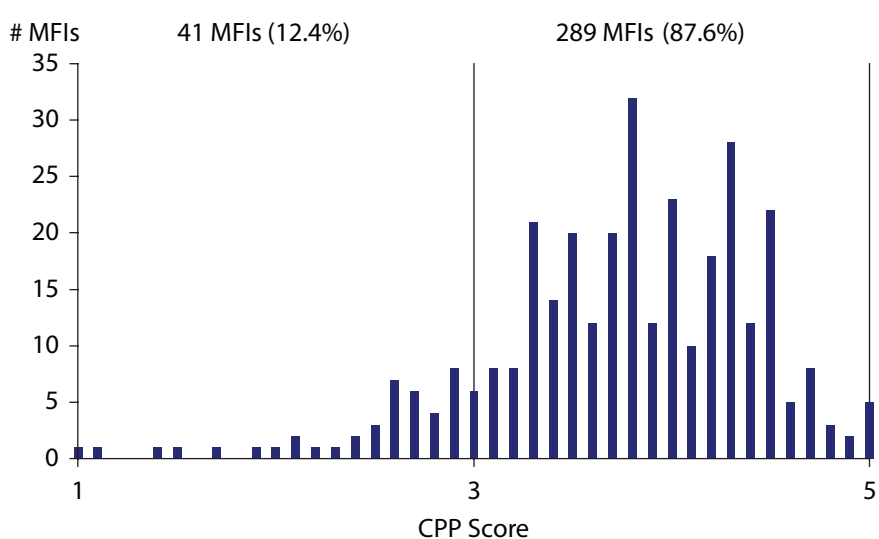
all client protection, Sub-Saharan Africa (SSA) is a notable exception, lagging behind in most measures of client protection (see Figure 3).

Because the sample for Africa is broad, with 75 independent observations covering 63 MFIs and featuring a broad distribution of evaluation sources, we believe this trend to be telling, even after accounting for the above-mentioned caveats. There are a number of possible explanations for this – the African microfinance market is generally less developed than others; it has more small MFIs than average; and its regulatory environment is generally weaker. We will be able to make more definitive statements when we have a more robust dataset, but these initial results are strong enough to warrant further research and perhaps increase the Campaign’s attention to Sub-Saharan Africa.

With the exception of responsible pricing, explored below, there is relatively little variation in scores by institutional type. A more pronounced differentiation can be found in institution size, where very small MFIs (<\$2 million in assets) demonstrate relative weakness in client protection. With only 13 MFIs in the category, this finding is preliminary, but it is bolstered by the fact that the next asset size category (\$2-5 million) also trails the rest of the sample.

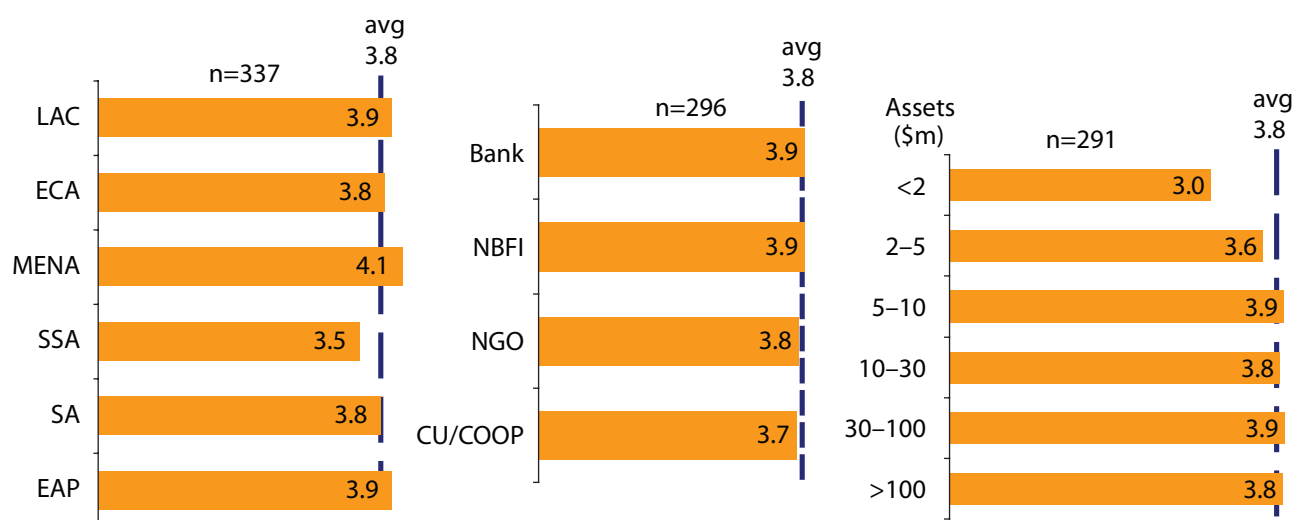
This suggests that client protection practices may either be sensitive to organizational scale or that it may

**Figure 2. Overall CPP Scores Are on the Positive Side**



Source: CPP Benchmarks.

**Figure 3. Combined CPP Benchmarks 0.1—Scores (all principles, weighted by number of observations)**



be easier to observe practices at larger institutions. Larger institutions have greater resources, which they can deploy by designating an individual or unit to be responsible for client protection. These units in turn drive changes in policies and manuals, provide training, and undertake other efforts to establish and improve client protection practices. Importantly, these activities can also be easily observed by on-site assessors. Small institutions often have less detailed and formalized policies and procedures, and their relationships with clients may also be less formal, while their actual practices may not be as easy to gauge during assessments. Moreover, formalization through policies is valued in the evaluation process

as an additional assurance that good practices are not incidental and left to the varied actions of individual staff members.

Nevertheless, the effect of scale appears to be limited. Consistently high scores by larger but still small MFIs (\$5–10 million), suggest that the benefits of size are not incremental. Nor is there any perceptible trend for MFIs above \$10 million in assets. It is possible that, once minimum scale is achieved (at around the \$5 million mark), client protection becomes driven more by organizational focus, with resources no longer being a significant limiting factor for developing client protection practices.

Part III. How MFIs Are Implementing the Client Protection Principles<sup>8</sup>

This section delves into the results of the CPP Benchmarks 0.1 principle by principle. It uses the same dataset as the previous section, augmented by mini case studies to examine how specific MFIs have been improving their client protection practices. Note that the “spider-web” chart at the top of each principle shows the average CPP Benchmark 0.1 score for that category.

Prevention of Over-Indebtedness

The Campaign describes over-indebtedness as the inability to handle debt service payments without sacrificing basic quality of life. Evaluations of this principle examine to what extent the MFI practices prevent the risk of over-indebtedness by verifying client capacity to repay and providing appropriate incentives to staff.

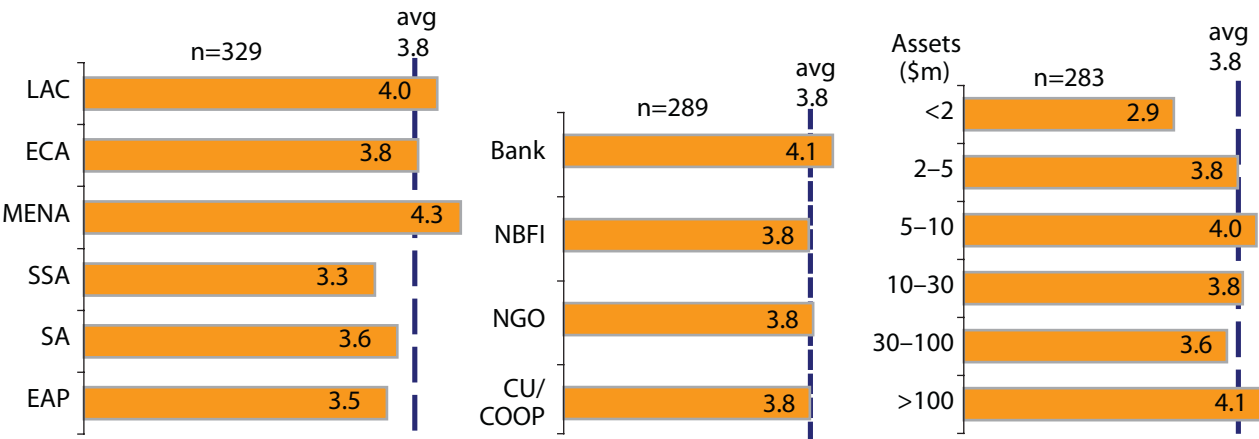
The Campaign focuses on the MFI’s ability to evaluate client repayment capacity, excluding collateral and guarantees. Instead, Campaign assessors look to assessments of client income, expenses, and outstanding debt, taking into consideration the local market context. The indicators also include other institutional factors that support prudent lending, including loan officer training and the extent to which staff incentives reward thorough client screening.<sup>9</sup>

Scores on prevention of over-indebtedness are relatively high compared to other principles, with the global average of 3.8 on a scale of 1-5, though as mentioned before, the absolute level should not be over-emphasized, given the preliminary nature of the CPP Benchmark 0.1 methodology. However, there are some notable category differences. Regionally, MENA and Latin America and the Caribbean score high, while Sub-Saharan Africa and East-Asia Pacific lag. An even stronger trend is evident in the association between institution size, with small MFIs (<\$2 million) substantially underperforming their larger peers (see Figure 4).

Although risk of over-indebtedness is closely related to credit risk, the two are not the same. An over-indebted client may still be able to make repayments by selling assets (including livelihood-generating assets), forgoing essential expenditures on food, and making other sacrifices that may result in decline in quality of life

8. Note that the principles listed below reflect an earlier version of the CPPs, before the version adopted in June 2011. This excludes the newly added principle of Appropriate Product Design.  
9. For a more detailed list of questions that should guide model practice for each client protection principle, see Appendix VII: “Getting Started Questionnaire.”

Figure 4. CPP Benchmarks 0.1—Prevention of Over-Indebtedness



or even impoverishment. The Smart Campaign will soon publish research from Ghana that finds many clients who perceive themselves to be over-indebted and making unacceptable sacrifices, even though they continue to repay on time.<sup>10</sup>

This may be one of the key reasons why, despite microfinance lenders' traditional focus on avoiding credit risk, over-indebtedness has been at the heart of several recent microfinance crises. This makes it doubly important to ensure that the methodologies used to assess MFI policies and procedures take into account the market context. Techniques that work in low-competition settings and good economic times may need to be adjusted when competition grows or the economy stagnates.

Raters and investors are already paying closer attention to over-indebtedness when they assess MFIs than they do for some other CPPs. Many ask deeper questions, including the maximum share of client disposable income allowed to count toward repayment coverage and the number of existing loans held by clients. These questions begin to reflect the recognition that, in some markets, conditions warrant adjustments in credit policies to address multiple lending. Thus, client protection assessments need to recognize that practices that successfully avoid

over-indebtedness in low-competition settings may require additional support in high-competition ones, including the use of credit bureaus or limits on the number of institutions a client can borrow from at any one time.

One example of this is the unrelenting focus of AccessBank Azerbaijan on carrying out detailed client evaluations, backed by an emphasis on portfolio quality incentives, which has created an environment where over-indebting clients is unlikely. The result has also given AccessBank one of the lowest delinquency rates in the country (see Box 3).

That said, an important caveat to consider is that too strong a focus on achieving low delinquency through incentives is that it may encourage over-aggressive collections practices, violating the principle of fair and respectful treatment of clients. One mechanism to overcome this tension between the principles is to separate the staff responsible for client evaluations and collections into separate units, each with its own incentives. This would ensure that incentives for thorough client selection can only affect the evaluation process, with collections efforts being driven by a separate set of metrics. However, this approach has not been implemented by AccessBank.

The flip side of emphasizing portfolio quality through incentives is that it lowers incentives for growth and

10. Jessica Schicks, forthcoming.

### Box 3. Setting Standards to Prevent Over-Indebtedness at AccessBank, Azerbaijan

When it comes to client ability to pay, AccessBank takes an in-depth assessment approach. Its loan officers are strongly encouraged to conduct detailed evaluations of client repayment capacity. This encouragement is backed by an incentive scheme that heavily emphasizes portfolio quality: For every 1 percent in portfolio delinquency, a loan officer loses a substantial portion of his or her bonus – a bonus that constitutes a large portion of total compensation. Portfolio performance is likewise a key component of management incentives as well.

Unsurprisingly, loan officers conduct extra-thorough client evaluations. For example, in smaller towns or close-knit neighborhoods, loan officers seeking to verify whether clients are telling the truth about their financial situation will tap their own personal networks to learn whether the client may have other loans. Loan officers also check with counterparts at other MFIs and banks. Finally, staff run a check through the country's credit bureau, which in 2011 was expanded to include MFIs.

AccessBank supplements its field-level efforts with thorough portfolio analysis. It has invested heavily in building up a risk management unit, now 10-person strong, which helps identify potential weaknesses in the client evaluation process.

Finally, AccessBank has been spearheading a campaign to reduce over-indebtedness at the sector level. Collaborating with the Azerbaijan Microfinance Association (AMFA), AccessBank has been seeking to promote a "one-client, one-lender" strategy, where a lender seeking to provide a second loan to another MFI's client would commit to pay off the client's existing loan. Thus, if a lender wishes to issue a \$3,000 loan to a client who already has \$5,000 outstanding with another lender, that new lender would have to issue an \$8,000 loan, part of which would go to pay off the client's outstanding debt.

productivity. Indeed, given current lending methodologies that emphasize face-to-face interaction, high client-to-loan officer ratios are simply inconsistent with the depth of evaluation necessary to assure that borrowers have sufficient capacity to repay, especially when credit bureau data are limited. Thus, MFIs with high loan officer case loads may find it difficult to implement reasonably strong over-indebtedness protections without reducing loan officer case loads.

While lenders bear much responsibility for avoiding over-indebtedness, clients also have a responsibility to borrow prudently. Unfortunately, not all borrowers have the understanding and sufficient caution to avoid falling into risky situations that can lead to over-indebtedness. Moreover, research in behavioral economics suggests that over-optimism about the future (leading to overly risky borrowing) is an inherently human trait. Client education to make people more aware of the dangers of over-indebtedness is one approach to countering this tendency.

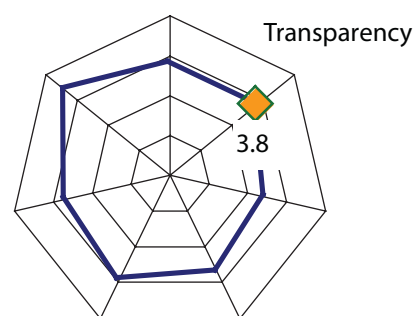
This was the path taken by Ujjivan in India. In response to the growing frequency of practices among MFIs in southern India such as multiple and ghost

borrowing, Ujjivan developed an educational film and translated it into 12 regional languages (see Box 4). It has by now been shown to more than 1 million viewers. The response has been highly positive. After seeing the film, many of Ujjivan's clients ask: "Why did you not show this to us earlier?"

## Transparency

In order to meet their commitments to transparency, lenders must communicate clear, sufficient, and timely information in a manner and language clients can understand so that the clients can make informed decisions.

As with prevention of over-indebtedness, every rater and assessor contributing to our dataset included transparency, and as a result the dataset includes 328 observations on this principle. Scores for transparency are generally



### Box 4. Sushila and Revati Help Ujjivan Teach by Example

Facing a growing incidence of multiple borrowing (clients taking simultaneous loans from different providers) and ghost borrowing (clients taking out loans for others, in return for a commission), Ujjivan developed an educational video highlighting the risks of these practices. Featuring the characters Sushila and Revati, rural women who represent typical microfinance borrowers in India, the video teaches by example.<sup>a</sup>

In the first segment, a respected relative visits Sushila and her husband and convinces them to take out a large loan in Sushila's name and hand him the proceeds, which he promises to repay punctually. Soon after, he vanishes, leaving Sushila stuck with repayments she cannot afford.

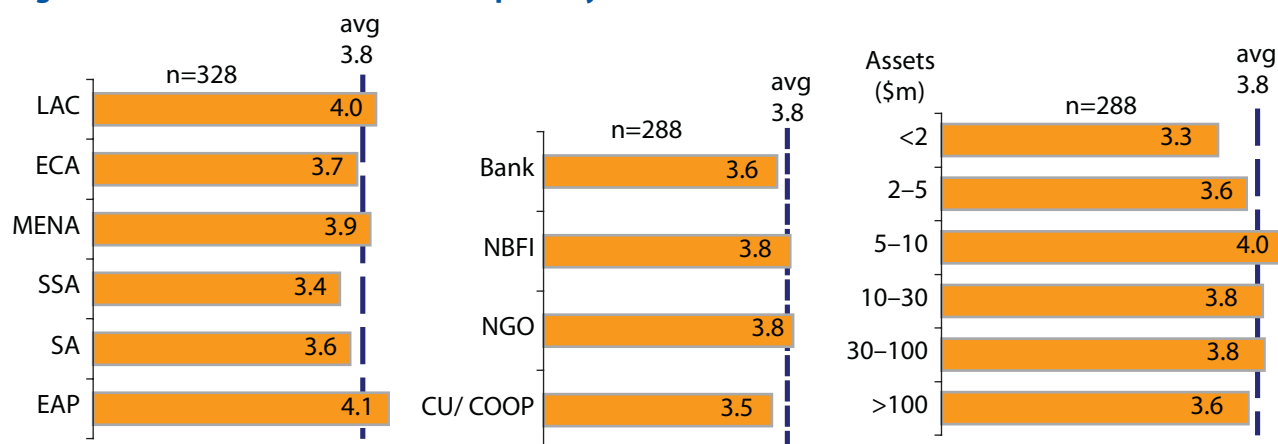
The second sketch shows Revati, a microfinance client who is bullied by her husband into taking out a second loan so he can buy a motorbike, and a third loan to make the repayments. Soon after, they find themselves unable to repay.

The two vignettes are simple, but Ujjivan reports that clients watch the videos with unusual focus, and follow them with highly animated discussions. Clients appear to identify readily with Sushila and Revati, whose dealings with overbearing husbands and relatives closely reflect the family dynamics they see in their own homes. The film also introduces clients to the concept of a credit bureau and educates them on the importance of building a positive credit history, an important factor given the launch in mid-2011 of credit bureau coverage for Indian MFIs.

Within its first year, Ujjivan showed the film to more than 1 million families, through local television channels as well as during its own client meetings, where it follows up with a guided discussion. The video is now mandatory for all new Ujjivan clients and staff, and represents a notable contribution toward avoiding the types of issues that have plagued Indian microfinance in recent years.

a. For an English-subtitled excerpt, see <http://www.youtube.com/watch?v=VIKfIRlcSaY>.

**Figure 5. CPP Benchmarks 0.1—Transparency**



high, although Sub-Saharan Africa and small MFIs are lagging. Aside from these, there are no notable deviations from the average (see Figure 5).

The primary focus of transparency is communicating product information in a way that allows clients to make informed decisions before borrowing or opening an account, particularly information about pricing. The core component of transparency is pricing disclosure, including how clearly and understandably a provider presents interest rates, fees, and commissions; required purchases (such as insurance); minimum savings balances; other factors that affect the economic value of a loan or other product; and to what extent the resulting pricing can be compared across different lenders. This also means communicating effectively with clients

who may not be literate. Moreover, commitment to transparency continues after the initial loan disbursement or savings deposit, with ready provision of account statements and responsiveness to balance verification requests.

Microfinance institutions can gain from providing more transparent disclosures. Clients may value those lenders who provide more information in a clearer format over those whose pricing disclosure is obscure. One example of an MFI taking this approach is Gatsby in Uganda, which has developed a loan repayment schedule that simply and clearly communicates all key information to the borrowers. Such disclosure has allowed Gatsby to communicate all relevant loan information to its clients quickly and efficiently (see Box 5).

#### Box 5. Gatsby Shows All

In the microfinance market in Uganda, non-transparent disclosures are the norm. There is no single point of reference that clients can consult to understand their loan pricing structure. Loan repayment schedules often fail to include interest rates, fees, commissions, and other pricing components.

In this market, one MFI, Gatsby, has developed a repayment schedule that truly stands out. On a single sheet of paper, Gatsby has been able to display a wealth of information regarding the loan, and do so in a well-laid-out manner that is clear and understandable. The schedule shows all loan fees and commissions, the interest rate and its calculation method (flat rate), the repayment grace period, a full repayment schedule that breaks out interest and principal installments, including those due and still to be paid, and the total amount of interest to be paid over the life of the loan. The schedule also includes important reference information, such as the loan officer's name, branch contact information, as well as the date the schedule has been generated.

One major benefit to Gatsby is that in a market where a loan officer appropriation of client repayments is not infrequent, clients now have a clear document that lays out exactly what they have paid and what they owe. Similarly, sharing a wealth of loan pricing information allows clients to understand their loan better. Such transparency allows Gatsby to build greater trust with its clients, and thus constitutes an important advantage over its competitors.

Source: Courtesy of MFTransparency.



However, providing complete information is not always enough. One of the difficult factors in presenting pricing for financial products is that it is inherently complex. Few clients, whether educated or not, can evaluate the difference in interest cost presented through a “flat-rate” or “declining-balance” method, yet the difference of the actual interest paid for the same stated percentage can vary by a factor of two. Fees, minimum balances, loan tenors, and other factors further affect the price paid or the actual loan proceeds received. A recent industry effort, *MFTransparency*, has developed tools that allow lenders to calculate pricing using a standardized methodology (such as APR or EIR),<sup>11</sup> which incorporates all product terms that impact pricing, allowing clients to compare pricing among different products and different providers.<sup>12</sup>

When it comes to communicating pricing information, market dynamics are a critical component to lender transparency. Institutions that seek to present transparent pricing in a market that does not require full, standardized forms of disclosure may be penalized in the marketplace if their prices appear higher than those presented by less transparent competitors. Clients may not even be aware that rates are being presented in different ways. As consensus builds among regulators and providers toward regulating full disclosure, an important area of focus is on how best to shift the industry toward more easily comparable standards.

However, government regulation is not always the sole means of moving the market toward improved practices. Examples in other industries demonstrate that when a group of dominant market players agree on forms of disclosure or a single set of standards, market forces can sometimes force the rest of the sector to adapt. The approach of *MFTransparency* is to collect full pricing information from all or nearly all MFIs in a given country and publish the information in a comparable format. Once this process reaches critical mass, it is possible that participation in *MFTransparency* data collection may become a mandatory requirement of microfinance networks, donors, and socially responsible investors. The re-

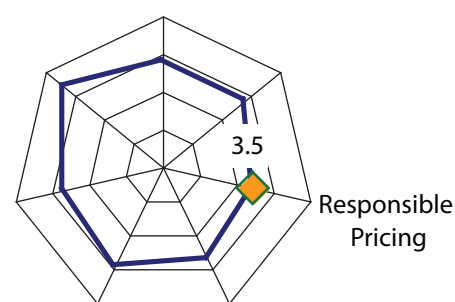
sulting external demand makes it easier for all players in a given market to take the big step toward full and standardized disclosure together, without advantaging or disadvantaging any one provider. However, such a path is not guaranteed, as it cannot address continuing non-comparable disclosure used by other providers that are not dependent on such outside support.

## Responsible Pricing

This principle requires financial institutions to set prices, terms, and conditions that are affordable to clients while recognizing the need to maintain their own sustainability.

When compared to large loans provided by banks, microcredit can be expensive. This is largely a factor of microfinance economics that combine small

loan sizes with hands-on interaction with the client. The result is higher operating costs that have to be covered through higher interest and fees. Those higher costs often become a subject of controversy, in which politicians, the media, and the public at large frequently take a negative view of MFI interest rates and, by extension, of the MFIs themselves.



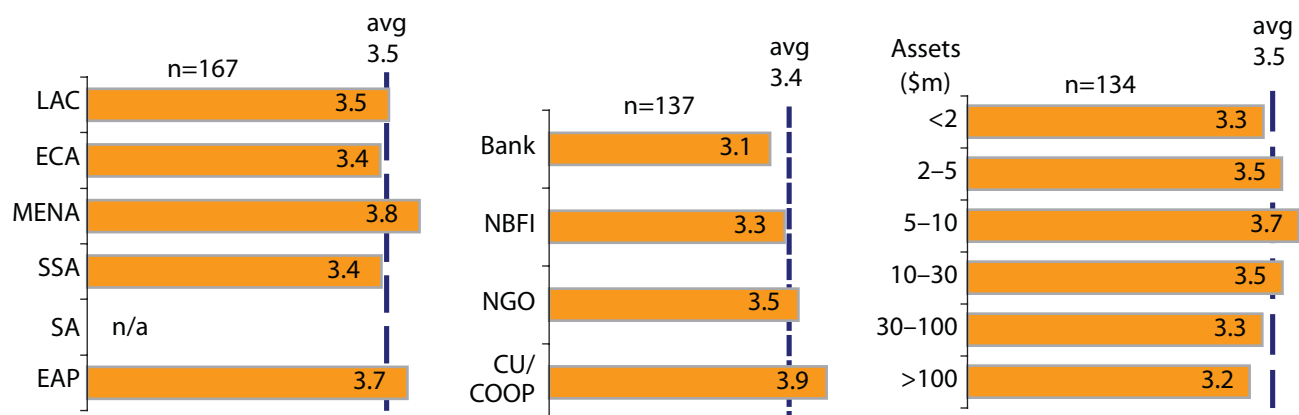
In our dataset, only four out of six CPP Benchmark contributors provide a separate score for responsible pricing. This is in part due to the complexity of the issue. Multiple factors go into a responsible price – the efficiency of the provider, decisions about profitability, cost of business, size of loans, and of course the pricing itself. These factors interact with each other, and are moreover highly context specific, making it difficult to set specific price guidelines.

Based on CPP Benchmark 0.1 data, scores for responsible pricing make it the lowest-scored CPP Benchmark category, with an average score of 3.5. The range of scores is also rather narrow, especially at the regional level. However, institution type shows heavy variation, with credit unions scoring well above other types of organizations, while banks

11. APR = Annual Percentage Rate; EIR = Effective Interest Rate.

12. For more information, see <http://www.mftransparency.org>.

**Figure 6. CPP Benchmarks 0.1—Responsible Pricing**



score well below. Meanwhile, mid-size organizations score best on this principle, with scores dropping off for both larger and smaller providers (see Figure 6).

When evaluating responsible pricing, the Campaign’s assessors benchmark an MFI’s prices against its peers, using data from *MFTransparency* where available, and supplement with efficiency and profitability data from the MIX ([www.themix.org](http://www.themix.org)) and other sources. Where *MFTransparency* data are unavailable, portfolio yield and other proxies for price are used instead.

Generally, the presence of high prices and low efficiency ratios, without an explanatory factor (for example, the MFI makes very small loans or focuses on rural areas that are more costly to serve), suggests that the MFI may be charging clients for its own inefficiency. Similarly, the combination of high prices and high returns on assets, without other explanatory factors, may indicate that an institution is generating excessive profits.

A closer examination of scores in this dataset suggests that pricing (using portfolio yield as proxy), operating expense, and profitability ratios all follow strong trends, with all three decreasing as institutions get larger (Table 4). However, there is one notable exception: middle-range MFIs (\$5-10 million assets) have relatively low prices, along with moderate expenses and moderate profitability. This group also receives the highest Responsible Pricing Scores in the CPP Benchmarks 0.1. The picture is less clear for low-scoring large institutions (>\$100 million), which have the lowest prices, operating expense, and profits, but also the lowest scores. It is unclear why this should be the case. Part of the difference may be attributable to the diversity of market contexts that are not readily apparent.

Pricing disclosure makes it more difficult for high-cost providers to hide behind hidden charges and fees. Simultaneously, at the market level, transparency encourages price competition, which tends to bring down costs – and price. From the Campaign’s

**Table 4. Responsible Pricing Follows Financial Ratios (n = 96, avg)**

ASSETS (\$M)	APPR. PRICE SCORE	PORTFOLIO YIELD (REAL)	OPER EXP/ ASSETS	PROFITABILITY (ROA)
<2	n/a	n/a	n/a	n/a
2-5	3.5	30.4%	27.2%	8.5%
5-10	3.8	24.3%	16.4%	3.7%
10-30	3.6	28.1%	19.8%	5.8%
30-100	3.4	26.1%	15.0%	4.1%
>100	3.3	20.7%	10.4%	3.0%
<b>Total</b>	<b>3.5</b>	<b>26.0%</b>	<b>18.6%</b>	<b>5.6%</b>

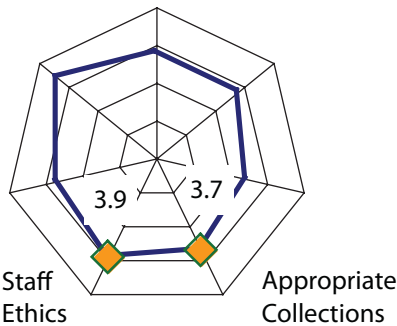
Source: CPP Benchmarks, MIX Market (financial ratios).



perspective, transparency is a key precondition for ensuring Responsible Pricing practices.<sup>13</sup>

### Fair and Respectful Treatment of Clients

This new principle combines into one all the elements that address how clients are treated in direct interactions with providers. As part of the June 2011 revision of the principles, two of the original principles – Appropriate Collections Practices and Ethical Staff Behavior – have been combined into a single principle, Fair and Respectful Treatment of Clients. In addition, the new principle has been expanded to include the concept of non-discrimination.<sup>14</sup>



Given that the principles have only recently been revised, most of the Smart assessments and all of the third-party evaluations were based on the original version two-part version of this principle.

Both parts of this principle receive significantly less attention than transparency or prevention of over-indebtedness, with only two of the five polled invest-

13. For more detail, please see the December 2009 paper “Responsible Pricing: The State of Practice” in the Tools section of the Smart Campaign website.  
 14. For detailed guidance about the revised principles, click here or see the Client Protection Principles page on [www.smartcampaign.org](http://www.smartcampaign.org).

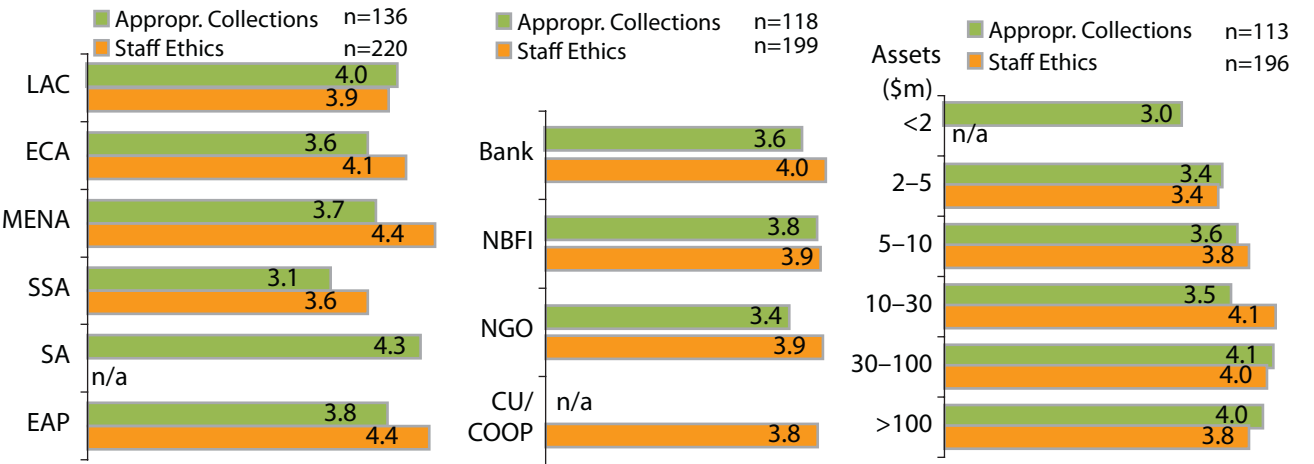
ment managers including validation of each component in their social due diligence, though it is included by both social raters.

Providers scored well on both parts of this principle relative to their scores on other CPPs, with ethical staff behavior being an especially strong standout. These high marks appear to contradict a number of recent public critiques of microfinance, in which heavy-handed collections practices have been especially prominent (alongside over-indebtedness and high interest rates). Perhaps the most notable case is the 2010 government action against microfinance in Andhra Pradesh, India, which explicitly cited MFI collections practices as the cause behind an alleged suicide spike in the state.

In addition to reiterating that this initial version of the CPP Benchmarks is only indicative and not a reliable measure of MFI performance generally, in this context specifically one should note that the South Asia sample is particularly small (eight MFIs) and not representative of the broad spectrum of Indian MFIs. As is the case elsewhere, Sub-Saharan MFIs lag behind in both categories, and very small MFIs (<\$2m) do poorly on Appropriate Collections Practices (see Figure 7).

At the heart of treating clients fairly and respectfully is a corporate culture that internalizes these values, with the appropriate tone set from the very top. However, a corporate culture, especially in an organization of size, cannot depend solely on the values promoted and practiced by management.

**Figure 7. CPP Benchmarks 0.1—Appropriate Collections and Ethical Staff Behavior**



To ensure that client respect is practiced consistently, organizations must clearly spell out prohibited actions in their employee handbooks. At a basic level, this assures that field staff will have a common understanding of how they should behave toward clients, and avoid situations where they must rely on their own notions of appropriate behavior, which can vary widely among staff. Prohibited behavior should also be backed by sanctions, up to and including firing of the employee and, in particularly egregious cases, turning the employee over to law enforcement authorities.

It is equally important that mechanisms be put in place to monitor staff behavior, such as providing channels for fielding customer complaints (see Mechanisms for Complaint Resolution, below), empowering internal audit to include assessment of staff behavior, as well as developing strong whistleblower protections that encourage staff to speak up when they see inappropriate behavior.

However, fair treatment of clients need not stop with prohibiting behavior and implementing negative sanctions. One Indian institution, Arohan, has gone a step further and used its interaction with clients as a means to distinguish itself from the competition (see Box 6). Its focus on punctuality demonstrates a degree of respect for clients that separates it not only from the competition, but also from most organizations its customers deal with on a regular basis.

The most difficult issues in client treatment usually come up during the collections process. Seeking to collect repayments from a client who may be unable or even unwilling to repay can involve a tense interaction. When not bound by clear expectations of allowed and prohibited behavior, it may escalate to abuse or harassment by the field agents or other staff. The potential for wrongdoing may be further aggravated when staff incentives are tied to maintaining low delinquency levels or to maximizing recoveries.

But avoiding harassment may not be sufficient on its own. For overdue loans specifically, an important component for assessing fair and respectful treatment of clients is whether an MFI has a mechanism for rescheduling loans in specific cases when clients face serious financial difficulties that make timely repayment impossible. Moreover, it is important that such rescheduling be made on a case-by-case evaluation of the client's situation, and not be made on a blanket or formulaic basis, which may instead indicate an institution attempting improperly to reduce its reported delinquency rate. Even when blanket rescheduling is done in good faith, as for example after a natural disaster, the approach is still likely to miss the nuances of each client's specific situation, with some clients requiring greater flexibility than others.

At FMM Popayan, when one of its service areas was affected by severe flooding, staff and the CEO took

#### **Box 6. Arohan's Clockwork Microfinance**

For India's poor, waiting is a way of life. Waiting at government offices. Waiting for trains. Waiting at banks. In this environment, the microfinance provider Arohan saw an opportunity to distinguish itself. "Arohan is here, must be 11am!" joke its clients. And indeed, such is the punctuality of its staff that one could literally set the watch based on their arrival.

Arohan has institutionalized the notion of treating its clients with respect. The most visible of these is timeliness, which is listed as one of Arohan's core values and is included as part of staff training. It is normal for staff to arrive at the location a few minutes early, then wait until the exact appointed time before entering the meeting place or the client's place of business. That the clients react positively to such treatment is self-evident. But the benefits to Arohan go beyond a positive brand image.

On-time arrival by staff is mirrored by that of the clients. Coupled with Arohan's practice of structuring its loan repayments always to be in increments of 50 rupees, its focus on timeliness substantially improves its collections efficiency. In an environment where many of its competitors spend 30-60 minutes during collections, Arohan's loan officers spend only 15.

The image of efficiency and professionalism is a point of pride for the staff as well – Arohan's expectations for professionalism and timeliness aside, the positive feedback and respect they receive from clients constitute an important motivating factor in its own right.

a boat to visit the affected area and meet with the clients. For clients, this demonstration of interest in their situation was on its own an important demonstration of commitment. Following this visit, field staff met with each borrower to assess her specific situation and tailored the loan restructuring toward her needs, ranging from extending the loan term for a few months to issuing a new loan for a client whose business premises were washed away and required rebuilding from scratch.

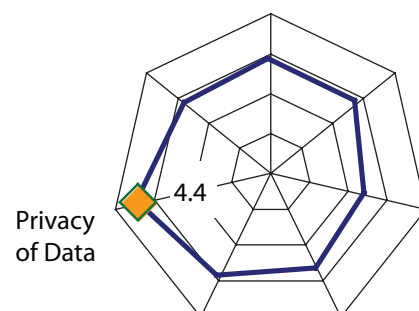
After revamping its collections process, FMM Popayan also found that it had less need to resort to the judiciary in order to repossess defaulted clients' property (see Box 7). Nevertheless, asset seizure can sometimes be necessary, and here it is important that responsible lenders have clear guidelines of what constitutes an acceptable asset for repossession. Assets that are strictly consumer goods, such a television, can constitute suitable collateral in cases where clients are unable or unwilling to repay their loans. However, an asset that is essential for the client's basic livelihood is more problematic. For example, a microwave, while normally considered a consumer good, may still be out of bounds in the case of a

client who runs a food business. In evaluating the MFI's commitment to the principle of fair and respectful treatment of clients, the Smart Campaign does not predefine what is or is not acceptable collateral, as this varies by country, region, and client segment. Instead, Campaign assessors evaluate the guidelines employed by the MFI that list allowable and prohibited assets to see whether they are specific and clear.

### Privacy of Client Data

The core of the privacy principle is the acknowledgment that client data belong to the client, and not the institution, and that misuse of the data has the potential to harm clients.

Both staff and clients should know how client data will be collected and used, and client data should be protected in accordance with the minimum requirements of the country – and often beyond. As a general rule, lenders should recognize that sharing



### Box 7. Treating Defaulters with Dignity at FMM Popayan

In late 2008, FMM Popayan's management was facing a dilemma. Delinquencies were rising across the board, field staff were increasingly reporting difficulties in their collections, and the institution was receiving increasing numbers of complaints from its customers as relationships with collections staff grew increasingly more strained. Naturally, FMM Popayan needed to make sure its loans continued to be repaid, but it didn't see the deteriorating relationship with its clients as a helpful means to getting there. Management knew that it needed to change its collections practices. The question was, how?

They decided to ask the clients. The feedback they received proved enlightening. Clients told FMM Popayan that they didn't like collections being done after dark. They didn't care for the disrespectful attitude of some of the loan officers. But mainly, they said that they needed a more understanding approach to collections, and more payment flexibility in the event their own businesses were facing difficulties. In parallel, FMM Popayan consulted with its best-performing loan officers to learn the strategies they were using.

The outcome of the exercise was a collections manual that clearly spelled out what field staff should and shouldn't do when dealing with delinquent clients. Collections after dark were out. Dress that was suitable to the client's milieu (e.g., rural trader vs. urban small or medium enterprise) was in. Collecting for delinquent loans in public spaces was out. Discussing repayment issues in private rooms at the MFI branches was in. SMS texts to communicate repayment details was in, but only through standardized templates that treated clients with respect. Individual messages written by the loan officers were out, as were text messages after dark. Meanwhile, the MFI's methodology coordinators saw to it that the new collections policies were followed consistently in all its branches.

FMM Popayan also revised its methodology for loan rescheduling, which allowed for individualized evaluation of the client's situation rather than blanket demands for repayment. With the new policies, FMM Popayan noted that it was able to keep delinquency levels low while substantially reducing the frequency with which it had to resort to judicial action in order to repossess client assets. As it turned out, in most cases a positive relationship with clients proved more effective than strong-arm tactics.

client data should be done with client acknowledgment and based on clear, understandable disclosure (no legalese). Clients should not be asked to waive their privacy rights unless genuinely necessary.

Privacy of client data is the least monitored principle, with only one out of the five investment managers including it in their social due diligence questionnaires. The resulting scores are thus heavily weighted toward one manager's methodology, which is somewhat divergent from the norm and features generally high scores. Thus, data privacy scores should not be compared with scores of other CPPs.

Within privacy of data itself, there are no pronounced trends, with the slight exception of the Europe and Central Asia region, which scores higher than average, while East Asia and Sub-Saharan Africa scored below average. Some of this variation may be attributable to generally greater regulatory requirements in the ECA region, which normally incorporate client privacy guidelines (see Figure 8).

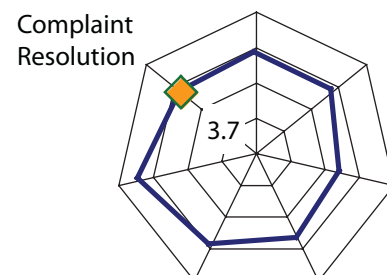
One notable exception to privacy requirements is reporting to credit bureaus, which is often mandatory. Given the importance of credit-reporting information for safe lending and prevention of over-indebtedness, it is not a violation of privacy for a lender to refuse to do business with clients who are unwilling to authorize the lender to share their data with a credit bureau. In many countries, reporting to a credit bureau is mandatory altogether, in which case privacy requirements are reduced to client notification, rather than client consent.

Other aspects of safeguarding client data apply to information technology security, as well as maintaining paper data (such as loan folders) in a secure location. Practices such as loan officers taking client folders home are a violation of data privacy, even when well intentioned. Perhaps the most common complaint in the treatment of client privacy is the penchant of MFIs to consign information-sharing notices, including for credit bureaus, to legal jargon embedded within long loan agreements that are hardly ever read, let alone understood, by clients. In doing so, MFIs miss out on an important opportunity for educating clients about maintaining good credit histories, and thus improving their creditworthiness.

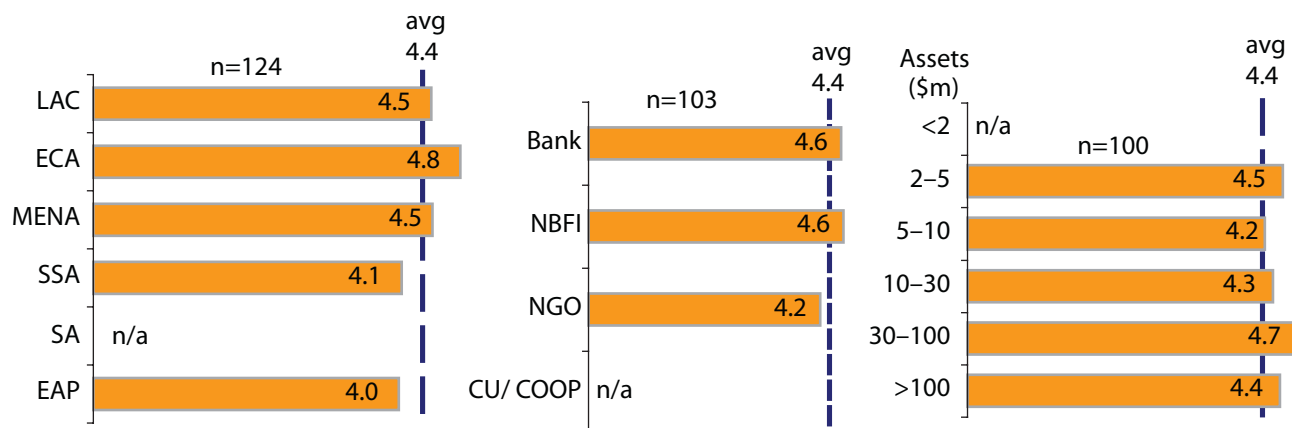
There are, however, some exceptions. One example is the film produced by Ujjivan (see Box 4 above), which explains the concept and importance of a credit bureau, emphasizing the importance of building a positive credit history. This effort to educate clients about the concept of a credit bureau distinguished Ujjivan from its peers.

### Mechanisms for Complaint Resolution

Ensuring that clients are protected requires that the institution have in place a mechanism for handling client complaints. This is a critical feedback mechanism that lets



**Figure 8. CPP Benchmarks 0.1—Privacy of Client Data**



clients resolve specific problems and share their concerns, including when they have been mistreated by a member of the MFI’s staff or don’t understand the terms and conditions of products.

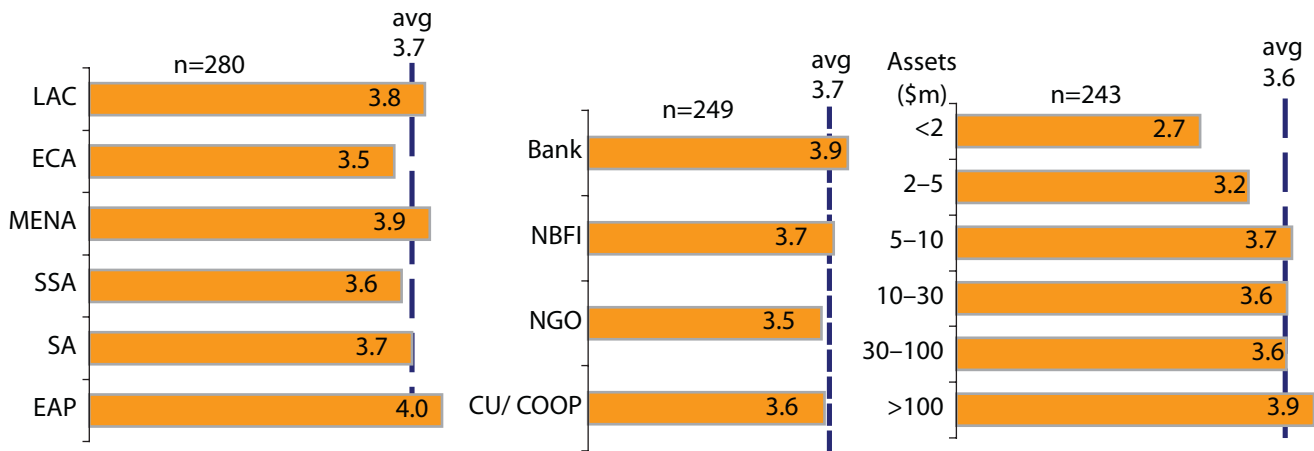
The overall average score for mechanisms for complaint resolution puts it in the middle of other Client Protection Principles. Distribution patterns are not especially prominent, with the notable exception of small MFIs, which lag well behind the average. Very small MFIs were the only group to score below the acceptable range. As with other CPPs, this may be a function of the relative informality of operations among very small institutions. Managers of small institutions may believe that problems can be resolved without specific policies and procedures (see Figure 9).

A complaints resolution mechanism is much more than a suggestion box. It requires that resources be assigned to handling complaints, backed by clear policies and procedures. There should be a clear path to decision-makers with the authority to resolve the issues raised in the complaints. The complaints channel should handle communication confidentially, efficiently, and reasonably quickly, and the institution should monitor received information as a source of valuable feedback for future service improvements.

But before any of these practices can be activated, a complaints process must first be used, and thus the complaints channel must be clearly and actively communicated to clients. Rolling out a complaints resolution channel must overcome the frequent reluctance of most poor clients to complain to an institution that provides them with needed capital. In short, clients must feel empowered to complain without fear of retribution. As many well-meaning MFIs may have found, reluctance to complain to the institution can be very strong indeed. Many a researcher, assessor, or third-party evaluator who has spoken to clients can probably recall incidents when a client complained about something she didn’t like, adding the requisite “please don’t mention this to X,” where X may be a loan officer, collections agent, or the MFI in general.

One lender that seems to have been able to overcome this barrier is Fonkoze in Haiti. When rolling out its complaints hotline, Fonkoze actively leveraged its organizational structure, introducing the hotline during its General Assembly meeting, then holding multiple sessions with regional and local client groups, and at each stage explaining client rights when using the hotline (see Box 8). Fonkoze backed this direct communication with a widespread marketing campaign that included posters in branches, cards handed out by loan officers and branch tellers, and detailed fact sheets.

**Figure 9. CPP Benchmarks 0.1—Mechanisms for Complaint Resolution**





### Box 8. Alo, Fonkoze?

When Fonkoze was evaluating its client protection practices, its first step was to use the Smart Campaign's most popular tool – the "Getting Started Questionnaire" – to help identify its greatest gaps in client protection. The findings pointed to a lack of a client feedback mechanism as a significant issue. To a significant degree, this stems from Fonkoze's broadly distributed client network, with many of its loan officers traveling as much as two hours to clients located in remote areas. These loan officers may thus be the clients' only point of contact with Fonkoze, which places them in a position of power, along with the potential risk for abuse of clients it entails.

To Fonkoze, the obvious solution was to roll out a toll-free phone hotline that would provide a direct link to headquarters for even the most remote clients, nearly all of whom had a cell phone. Management negotiated agreements with multiple mobile providers to secure a short, easily memorable toll-free number. They also leveraged an existing internal call center, creating a detailed call script to facilitate the handling of the calls. Finally, Fonkoze established a committee composed of senior management to review cases raised through the hotline.

Rollout was marketed using Fonkoze's hierarchical network of client groups. Having first been presented during the annual meeting, the hotline was presented at regional meetings of center leaders (each center consisted of 25-50 women), then to the groups themselves. Loan officers were given business cards with the hotline number to hand out to clients, as were branch tellers. Posters were hung in branches, and center leaders were asked to relay the hotline information to the clients.

An important part of these channels was to educate clients about their rights: For example, clients had a right to know their interest payments, and a right to notify the institutions if they suspected they were being improperly treated by their loan officers. Similar communication was done for internal staff, many of whom had initial concerns that the hotline would undermine legitimate collections efforts, as clients would simply use the hotline to complain about legitimate collections. To counter this concern, it helped that the hotline was also open for internal field staff to raise concerns when traditional channels could not be used.

Having been piloted in six branches over the course of six months, the hotline has already scored some successes. Among the first 300 calls, one client complained about suspected fraud by her loan officer, which was subsequently confirmed by Fonkoze; another client complained that she hadn't received a reimbursement calendar, an operational oversight that served as a reminder to update procedures. Other calls may have been prosaic but still useful, and all helped resolve important issues for the clients who called.

## Part IV. What Comes Next? Certification and Other Challenges

The Smart Campaign has achieved much during its still-brief existence. The elements of client protection are widely known in the industry, and their importance is widely accepted. With this increasing attention, MFIs, investors, and other actors are bringing their practices in line with the Client Protection Principles. This work is taking place in hundreds of institutions and in every region of the world.

This report has provided some assurance that the current state of practice among microfinance institutions, as evaluated by independent organizations, already supports the basic tenets of client protection. But there is much more work to be done before the CPPs are fully embedded in the core of microfinance, and before clients around the world are fully assured of safe, respectful, and transparent treatment. Recognizing this, the Smart Campaign has an ambitious agenda over the next few years.

### Certification

The next major step for the Smart Campaign is the planned launch of client protection certification in early 2012, in partnership with the specialized rating agencies, Planet Rating, MicroFinanza Rating, M-CRIL, and MicroRate.

Third-party assessments of MFI client protection performance are essential for providing confidence about actual practices. Many such assessments are already being conducted, with the data in this report alone covering some 300 MFIs. However, the assessments done so far fall short of certifying performance. For example, Smart Campaign assessments, though detailed and thorough, are positioned as learning tools targeted mainly at MFI management and not made public. Investor assessments are part of due diligence exercises, likewise confidential. Only rating agencies have provided their views publicly, as part of social ratings. Even so, there has not been an explicit tie to the CPPs made in a consistent way from one rater to another. Certification will change this.

The purpose of certification is to provide a clear, definitive, and public opinion on whether an MFI adequately implements the CPPs. This will allow institutions to represent to their clients, regulators, investors, and the general public that they meet the minimum standards of client protection. For this reason, it is essential that the certification process have strong credibility. The availability of certifications should provide incentives to institutions to align their practices with the CPPs.

Starting in early 2012, institutions will be able to request Smart Campaign certification from one of the organizations licensed as certifiers by the Campaign. During the first year, the four specialized microfinance rating agencies, Planet Rating, MicroFinanza Rating, M-CRIL, and MicroRate, will be the only licensed organizations, in recognition of their unique position as raters, deep expertise, and especially because of the good will they have shown in working with each other and the Campaign staff to develop common methodologies for certifying client protection. Certification will be available in conjunction with financial or social ratings, and as a stand-alone offering. In future years, it is expected that additional entities may be licensed as certifiers in order to broaden the reach of certification.

Development of the certification program has required substantial effort from many people. In June 2010, the Campaign constituted a task force of more than 30 experts across the industry to guide the development process, and a technical working group to develop a unified methodology. This is a key component of the certification program, since only a clearly defined methodology can ensure that certifications issued by different organizations will actually mean the same thing.

The certification program is still in development, and many of the parameters of the program need to be validated through industry feedback and field testing, both of which will take place in the fourth quarter of 2011. Neverthe-

less, the Certification Task Force (see Appendix V for a list of members) has made great progress over the past year to identify the main pillars of the program and the indicators that will constitute the basis for the certification. The task force agreed that certification needs to recognize real achievement in client protection and provide incentive for financial institutions to improve their practices. The task force also recognizes that establishing the “minimum standards” that are often referred to when client protection is discussed in microfinance circles requires significant commitment and attention if the standards are to be meaningful. This cannot be limited to evaluations of an MFI’s policies and procedures alone, but must also include a sound client validation process. The fact that a financial institution has responsible practices should not be taken for granted, but rather celebrated as a true achievement.

### **Furthering Outreach and Effectiveness**

The Campaign will continue the work already under way to carry the CPPs deep into the global microfinance industry through associations and other support organizations. It will continue to provide training and assessments and will continue to equip a growing cadre of people who carry on this work.

In parallel, the Campaign will continue to develop tools and resources, as well as disseminate them broadly to potential users who can apply them. This will be facilitated by an effort to embed client protection elements in microfinance training courses on standard microfinance management. Extensive effort will be made to build out guidance and know-how related to new areas addressed by the revised CPPs. Among the topics in the pipeline are client protection in product design and delivery, agent and electronic banking, and microinsurance, as well as guidance related to non-discrimination.

### **Client Voice in the Smart Campaign**

Many of the participants in the Smart Campaign recognize an urgent need to incorporate clients into the Campaign. This will be a long-term and challenging task. The Campaign recently launched a task force on the client voice, which is taking on this challenge. The group has begun work on two initia-

tives. The first involves assembling client education materials that deal with client rights and responsibilities, vetting the materials, and making some of the best materials available on the Smart Campaign website. The second initiative involves developing a questionnaire and related guidance for gathering information from clients around client protection issues. This questionnaire will be deployed in several countries to learn more about client protection from the client perspective. With these initial steps, the Campaign will be better equipped to deepen the role of clients in the Campaign.

### **Protecting Clients at the Market Level**

Most of the efforts of the Campaign to date have focused on identifying and implementing good practices at the service provider level. But providers operate in a context. As research on practices has proceeded, it has become clear that market conditions play a critical part in determining whether clients are protected.

Market context is particularly relevant for the principles of transparency and preventing over-indebtedness. For example, in evaluating whether a financial institution takes adequate steps to prevent over-indebtedness, one indicator is whether the institution consults a credit bureau before approving a loan. Of course, this indicator can be applied only in markets where adequate credit bureau coverage is available to MFIs. Methods for assessing client capacity to repay may need to be adjusted in markets with a great deal of multiple lending, but to date, there is still little empirical data on the links between multiple lending, over-indebtedness, and default. Perhaps most worryingly, the scores reported here on avoiding over-indebtedness appear quite strong, at the same time as there is an increase in the number of markets with over-indebtedness problems. We need to be sure that the indicators the Campaign uses are robust enough to pick up on such issues.

On transparency, Smart Campaign assessments have noted a difference in transparency between providers in countries with strong pricing disclosure rules and countries without them. There may also be a link between low levels of transparency and the presence of interest rate caps.



All of these considerations signal a need for market-level action, whether it be to increase the availability of credit bureaus, work with *MFTransparency* to publish pricing data, or develop early-warning signals on market overheating.

Market-level action also requires engaging providers and regulators, among others. The Campaign has already developed relationships with 30 national microfinance associations, because of the key role these associations could play in working at the market level. CGAP has been engaging with regulators, and the Alliance for Financial Inclusion (a network of regulators) has recently formed a consumer protection working group. The Smart Campaign will develop an action plan in this area during the coming year.

#### **A Final Note**

The effort to embed client protection deeply in the microfinance industry is still young, but as this report demonstrates, it is thriving. Some organizations clearly stand out, others are working on improving their practices, and others still may have only recently discovered the Smart Campaign and the concept of client protection. There is little doubt that the state of the practice is improving. We at the Smart Campaign will continue working to deepen and strengthen the roots that have been planted over the past two years.

## Appendix I. Smart Campaign Steering Committee

Ranya Abdel-Baki, Executive Director, Sanabel Network, Egypt  
Clara Serra de Akerman, President, WWB, Colombia  
David Baguma, Executive Director, Association of Microfinance Institutions of Uganda (AMFIU), Uganda  
Essma Ben Hamida, Executive Director, Enda Inter-Arabe, Tunisia  
Anne Hastings, Executive Director, Fonkoze, Haiti  
Francisco de Hoyos, Executive Director, Prodesarrollo, Mexico  
Grzegorz Galusk, Executive Director, Microfinance Centre (MFC), Poland  
Patricia Gates, Senior Director, Communities of Practice and New Initiatives, USA  
Samit Ghosh, Managing Director, Ujjivan, India  
David Grace, Vice President, World Council of Credit Unions, USA  
Mathias Katamba, CEO, Uganda Finance Trust, Uganda  
Anne-Françoise Lefèvre, Head of WSBI Institutional Relations, WSBI, Belgium  
Paul Luchtenburg, Senior Operations Officer for Microfinance, IFC, Vietnam  
Asad Mahmood, Managing Director, Global Social Investment Funds, Deutsche Bank, USA  
Kate McKee, Senior Advisor, CGAP, USA  
Beth Porter, Policy Coordinator for Financial Inclusion, United Nations Capitol Development Fund, USA  
Hans Ramm, Financial Sector Development, Swiss Agency for Development and Cooperation, Switzerland  
Elisabeth Rhyne, Managing Director, Center for Financial Inclusion, USA  
Rupert Scofield, President and CEO, Finca International, USA  
Vipin Sharma, Managing Director, Access Development Services & Access MF Alliance, India  
Ben Simmes, Directory Social Performance and Financial Analysis, Oikocredit International, Netherlands

## Appendix II. Strategic Partnerships

NETWORK NAME	COUNTRY/REGION	LEVEL OF ENGAGEMENT**
ACCESS -ASSIST	India	2
AEMFI	Ethiopia	1
AFMIN	Africa Region	1
AMFA	Azerbaijan	1
AMFI	Kenya	1
AMFIU	Uganda	1
AMIR	Rwanda	1
AMSOFIPO	Mexico	2
APIM	Burkina Faso	1
APIM	Mali	1
APSFD-CI	Ivory Coast	1
APSFD-Senegal*	Senegal	NA
CAM	China	1
CMF	Nepal	1
Consortium Alafia	Benin	1
COPEME	Peru	2
Emprender	Colombia	1
FAMF*	Cape Verde	NA
FINRURAL	Bolivia	1
GHAMFIN	Ghana	1
MAMN	Malawi	1
MCPI	Philippines	1
MFC	Eastern Europe and Central Asia	1
Pakistan Microfinance Network	Pakistan	1
ProDesarrollo	Mexico	1
RADIM	Argentina	2
Red de microfinanzas del Paraguay	Paraguay	2
REDCAMIF	Central America Region	1
RFR	Ecuador	1
Russian Microfinance Network	Russia	1
Sa Dahn	India	2
Sanabel	MENA Region	1
YMN	Yemen	2
ZAMFI*	Zimbabwe	NA

\*In discussion.

\*\* Level 2 refers to associations that have committed to requiring their members to complete a client protection self-assessment with the Smart Campaign's "Getting Started Questionnaire", report to the MIX annually, and participate in CPP trainings. Level 1 associations encompass all of the above, but additionally are conducting a number of in-depth, third-party client protection assessments.

## Appendix III. Top 15 Tools on the Smart Campaign Website

RANK	TOOL NAME	NO. OF HITS
1	"Getting Started Questionnaire": Client Protection Self-Assessment for Microfinance Institutions	6,424
2	Client Protection Principles Training Series	4,221
3	Responsible Pricing: The State of the Practice	2,385
4	Microfund for Women: Client Business Evaluation Toolkit	2,007
5	Building Institutional Culture around a Code of Ethics at Compartamos	2,004
6	Smart Note: Collections with Dignity at FinComún	1,935
7	Smart Lending: Client Protection in the Individual Loan Process	1,840
8	Smart Note: Implementing an Industry Code of Conduct at PMN	1,805
9	Client Protection and Financial Education Simulation	1,751
10	How to Develop an Institutional Code of Ethics	1,673
11	Conducting Client Protection Assessments: A Guide	1,592
12	Smart Note: Facing Over-Indebtedness at Partner Microcredit Foundation	1,410
13	Banco Solidario: Loan Officer Training Manual	1,392
14	Complaints-Analysis Spreadsheet (FMMB)	1,309
15	Complaints-Handling Manual (Tamweelcom)	1,222

## Appendix IV. Smart-Assessed Microfinance Institutions

MFI	DATE	COUNTRY
AccessBank	April, 2011	Azerbaijan
Actuar Tolima	June, 2011	Colombia
Arohan	May, 2011	India
Banco Solidario	June, 2011	Ecuador
BancoSol	July, 2011	Bolivia
Caja Morelia	January, 2009	Mexico
Cantilan Bank	June, 2009	Philippines
Compartamos	January, 2009	Mexico
Credito con Educacion Rural - CRECER	August, 2011	Bolivia
FinComun	January, 2009	Mexico
Fundación Mundial de la Mujer Bucaramanga	April, 2011	Colombia
Fundacion Mundo Mujer Popayan	May, 2011	Colombia
Fundación Nuevo Amanecer	July, 2011	Colombia
FUNDESER	June, 2011	Nicaragua
IDEPRO	May, 2010	Bolivia
Kasagana-Ka	July, 2009	Philippines
Mi-Bospo	November, 2008	Bosnia and Herzegovina
NBCO TBC Kredit	May, 2011	Azerbaijan
Partner	January, 2009	Bosnia and Herzegovina
Proapoyo	April, 2011	Mexico
PRONTO! – Bautzen S.A. y Kedal S.A.	December, 2010	Uruguay
Saija Finance Private Limited (SFPL)	December, 2009	India
SMEP	February, 2010	Kenya
Socur S.A.- CREDITEL	October, 2010	Uruguay
STIMA SACCO	October, 2009	Kenya
Swadhaar FinServe	July, 2009	India
Ujjivan Financial Private Limited	February, 2010	India
YES SAMPANN	September, 2009	India

## Appendix V. Smart Campaign Task Forces and Their Members

### CERTIFICATION TASK FORCE

Isabelle Barrès,\* Smart Campaign – Chair  
Radhika Agashe, ACCESS Development Services  
David Baguma, AMFIU  
Ewa Bankowska, Microfinance Centre  
Pieter Bas Schrieken, Hivos  
JD Bergeron, Kiva  
Heather Clark,\* Consultant for the Smart Campaign  
David Dewez, Incofin  
Diana Dezso, the SEEP Network  
Sharon D’Onofrio – Observer, SPTF Network Group  
Alex Fiorillo,\* MFTransparency  
Laura Foose,\* SPTF Network Group  
Cara Forster,\* the SEEP Network  
Tricia Gates,\* the SEEP Network  
Samit Ghosh, Ujjivan  
Juan Manuel Grau, FMMB  
Micol Guarneri,\* Microfinanza Rating  
Sergio Guzman, Smart Campaign  
Aban Haq, Pakistan Microfinance Network  
Emmanuelle Javoy,\* PlanetRating  
Celina Kawas (and Miguel Arvelo), Women’s World Banking  
Cecile Lapenu, CERISE  
Asad Mahmood,\* Global Social Investment Funds, Deutsche Bank  
Kate McKee,\* CGAP  
Alok Misra,\* M-CRIL  
Jenny Morgan,\* the SEEP Network  
Leah Nedderman Wardle, Consultant for the Smart Campaign  
Micol Pistelli,\* MIX  
Jody Rasch, Moody’s  
Elisabeth Rhyne,\* Center for Financial Inclusion  
Senad Sinanovic, Partner  
Frances Sinha, EDA/M-CRIL  
Lucia Spaggiari,\* Microfinanza Rating  
Blaine Stephens – Observer, MIX  
Dr. Koenraad Verhagen, Argidius Foundation  
Sebastien von Stauffenberg,\* MicroRate  
Rebecca Waskey,\* MicroRate

\*Denotes the members who are part of the technical subcommittee of this task force, working to develop the certification indicators.

### CLIENT VOICE TASK FORCE

Charlotte Connors, Smart Campaign – Chair  
Radhika Agashe, ACCESS Development Services  
Leslie Barcus, Microfinance Opportunities

Susana Barton, ACCION  
JD Bergeron, Kiva  
Alex Fiorillo, *MFTransparency*  
David Garfunkel, Fonkoze  
David Grace, WOCCU  
Bobbi Gray, Freedom From Hunger  
Jesila Ledesma, MicroSave  
Rafe Mazer, CGAP  
Maria Perdomo, UNCDF  
Jessica Shicks, Independent Consultant  
Jami Solli, Consumers International  
Andrea Stiles Pullas, Banco Solidario

### **EVOLUTION OF THE PRINCIPLES TASK FORCE**

Kate McKee, CGAP – Co-chair  
Elisabeth Rhyne, Center for Financial Inclusion – Co-chair  
H.R.H. Princess Máxima of the Netherlands  
Aris Alip, CARD Bank  
Gail Buyske, Consultant to the task force  
Alex Fiorillo, *MFTransparency*  
Rosalind Grady, Independent Consultant  
Beth Houle, Opportunity International  
Anne-Françoise Lefèvre, World Savings Bank Institute  
Camilla Nestor, Grameen Foundation  
Beth Porter, UNCDF  
Larry Reed, Independent Consultant  
Ben Simmes, Oikocredit  
Bahia Tahzib-Lie, the Netherlands

### **TOOLS TASK FORCE**

Leah Nedderman Wardle, Smart Campaign/SPTF – Chair  
Susana Barton, ACCION  
Natalie Domond, Fonkoze  
Cornelia Laass, SEF  
Jackie Mbabazi, AMFIU – Uganda  
Nejira Nalic, Mi Bospo  
Beth Porter, UNCDF  
Hans Ramm, SDC  
Margaret Richards, Iris Center  
Katie Torrington, FINCA  
Gary Woller, Woller Associates

## Appendix VI. CPP Benchmarks 0.1

As noted at the start of this paper, CPP Benchmarks 0.1 represent a first attempt to look at client protection practices from a holistic perspective. They are drawn from source data that are disparate, often incomplete, and built on frameworks featuring significant variation in what indicators they evaluate, as well as what metrics they use to measure them. Because this was an exploratory effort, throughout the process a conscious choice was made to favor breadth of coverage over accuracy or depth. It is expected that the information gathered here will help inform future efforts to measure client protection across the industry.

The 479 observations in the compiled dataset have required a significant amount of processing in order to produce the CPP Benchmarks 0.1. This involved primarily two steps: 1) aligning the received evaluations for each CPP Principle, and 2) rescaling the score on a single 1-5 scale used by the Campaign.

### Mapping

The alignment process involved mapping different questions/indicators to the most appropriate consumer protection principle. Because the full number of indicators is substantial, the entire list is not included here. However, we provide some common examples and their mappings:

<b>Prevention of Over-Indebtedness</b>	<ul style="list-style-type: none"><li>• Do loan officers take detailed information on the client's ability to pay?</li><li>• What is the maximum amount of the client's disposable net income that the MFI will allow as monthly payments?</li><li>• What % of clients borrow from other MFIs or banks?</li><li>• Are loan officers incentivized to maximize volume of portfolio?</li><li>• Participation in a credit bureau and/or data sharing</li></ul>
<b>Transparency</b>	<ul style="list-style-type: none"><li>• How and what information do you provide to your clients, and at what moment? (before or after purchase)?</li><li>• Are all prices, terms, and conditions conveyed to clients in plain-language fashion and using language that they are likely to understand?</li><li>• Financial literacy [training provided] to clients</li></ul>
<b>Responsible Pricing</b>	<ul style="list-style-type: none"><li>• What is the average portfolio yield or prices vs. market average for the country?</li><li>• What is your effective interest rate? Which formula do you use and what do you include? (use APR tool from <a href="http://www.microfinancetransparency.org">www.microfinancetransparency.org</a>) [responses evaluate margins and the rate relative to others]</li></ul>
<b>Appropriate Collections</b>	<ul style="list-style-type: none"><li>• Does the MFI have fair, uncoercive collection policies?</li><li>• Does the MFI have guidelines that prevent abusive debt collection practices? (e.g., in manuals of policies and procedures, training materials)</li></ul>
<b>Staff Ethics</b>	<ul style="list-style-type: none"><li>• Ethical staff behavior, including anti-corruption and appropriate collections practices</li></ul>
<b>Complaint Resolution</b>	<ul style="list-style-type: none"><li>• Do you have systems in place to prevent the unethical treatment of clients?</li><li>• Do you have a dispute resolution mechanism or another venue for client complaints? What is provided as part of the grievance procedures? (phone number, manager, etc.)</li><li>• Does the MFI have responsive mechanisms for complaints? (e.g., complaints phone line, complaints boxes, special policies and procedures)</li></ul>
<b>Privacy of Data</b>	<ul style="list-style-type: none"><li>• Do you have systems in place to safeguard the privacy of client files – both in branches and in the MIS?</li></ul>



Note that in some cases a question may reasonably cover more than one client protection principle (for example, Transparency and Responsible Pricing). In such cases, the mapping was driven by the dominant principle in the question. Where no such judgment could reasonably be made, the data were excluded altogether.

### Rescaling

For each observation, multiple indicators mapped to a given principle were then aggregated with equal weight, such that there was one score per principle for each observation. The resulting scores were also rescaled to a 1-5 scale, with the lowest and highest scores corresponding to 1 and 5, respectively, while those in-between were equally distributed along the final scale. Thus, a source that used a 3-point scale of (0, 1, 2) would have been mapped as 0→1, 1→3, and 2→5.

One observed result of this rescaling was an apparent inflation of scores, with sources that used a scale of 4 or more points tending to have lower average results than those that used a scale of 3 or fewer points. This is largely because the threshold for giving the top rating in a precise scale (e.g., a 5 on a 5-point scale) is significantly greater than on a less precise one (e.g., a 3 on a 3-point one), and because high scores are more prevalent than low ones, the inevitable result of such rescaling is score inflation. At the same time, rescaling this closer to the median (to use the above example, mapping a 0→2 and a 2→4) would have likewise inverted this pattern. Given the limitations of comparing multi-source data, it was decided that mapping to the extremes was the least bad option.

### Selecting and Aggregating

There was significant overlap in the observed results, with 479 evaluations covering approximately 300 MFIs. There were two paths to this overlap: 1) a single source evaluating the same MFI multiple times (for example, a rating agency with multi-year ratings, or a fund manager reporting for different funds), and 2) multiple sources covering the same MFI. In the latter case, the best effort was made to match the MFIs reported, using country of origin and MFI name to make the best match. Despite these efforts, it is possible that, due to changed or different names (in some cases only acronyms were provided), not all matches were made accurately.

First, any observations dated before 2009 were excluded (this may still include older observations that had no explicit date attached). Out of the remaining observations, a total of 201 MFIs were mapped to the MIX, with another 40 named MFIs that could not be located on MIX, in most cases because they were either too new to report (as of 7 Sep 2011, most MIX data are still as of FY 2009) or did not report for other reasons.

Another 97 MFIs were provided on an anonymous basis, making matching impossible. These presumably result in some level of duplication in the final dataset. Based on the ratios of matches from other sources, we estimate that of these 97, between 30 and 60 MFIs have duplicate entries in the set.

Once duplicate MFIs were identified and pre-2009 observations excluded, the resulting matched observations were averaged for each principle. Finally, note that two of the sources had slightly outlying overall average scores (3.1 and 4.2), but as these are on the opposite sides of the spectrum, we decided that including the data on the additional MFI evaluations they covered was more valuable than the narrower score distribution gained by excluding them.

### Summary of Data

We present below a summary version of the resulting data, subdivided by a few notable indicators. Note that a minimum of five MFIs were required in order to present any aggregate value. Those below this threshold are marked as N/A.

**Table 5. Scoring on Client Protection Principles (avg)**

	NO. OF MFIS	OVERALL SCORE	PREVENTING OVER-INDEBTEDNESS	TRANS-PAR-ENCY	RESPONSBL. PRICING	APPROPR. COLLECTIONS	STAFF ETHICS	PRIVACY OF DATA*	COMPLAINT RESOLU-TION
		<b>n=337</b>	<b>n=329</b>	<b>n=328</b>	<b>n=167</b>	<b>n=136</b>	<b>n=220</b>	<b>n=124</b>	<b>n=280</b>
Lat. Amer. & Carib.	139	3.9	4.0	4.0	3.5	4.0	3.9	4.5	3.8
E. Europe & C. Asia	83	3.8	3.8	3.7	3.4	3.6	4.1	4.8	3.5
Mideast & N. Africa	14	4.1	4.3	3.9	3.8	3.7	4.4	4.5	3.9
Sub-Saharan Africa	63	3.5	3.3	3.4	3.4	3.1	3.6	4.1	3.5
South Asia	8	3.8	3.6	3.6	n/a	4.3	n/a	n/a	3.7
E. Asia / Pacific	30	3.9	3.5	4.1	3.7	3.8	4.4	4.0	4.0
<b>Global</b>		<b>3.8</b>	<b>3.8</b>	<b>3.8</b>	<b>3.5</b>	<b>3.7</b>	<b>3.9</b>	<b>4.4</b>	<b>3.7</b>
		<b>n=296</b>	<b>n=289</b>	<b>n=288</b>	<b>n=137</b>	<b>n=118</b>	<b>n=199</b>	<b>n=103</b>	<b>n=249</b>
Bank	30	3.9	4.1	3.6	3.1	3.6	4.0	4.6	3.9
NBFI	157	3.9	3.8	3.8	3.3	3.8	3.9	4.6	3.7
NGO	90	3.8	3.8	3.8	3.5	3.4	3.9	4.2	3.5
CU/ COOP	19	3.7	3.8	3.5	3.9	n/a	3.8	n/a	3.6
<b>Total</b>		<b>3.8</b>	<b>3.8</b>	<b>3.8</b>	<b>3.4</b>	<b>3.7</b>	<b>3.9</b>	<b>4.4</b>	<b>3.7</b>
<b>Assets (\$m)</b>		<b>n=291</b>	<b>n=283</b>	<b>n=282</b>	<b>n=134</b>	<b>n=113</b>	<b>n=196</b>	<b>n=100</b>	<b>n=243</b>
<2	13	3.0	2.9	3.3	3.3	3.0	n/a	n/a	2.7
2-5	26	3.6	3.8	3.6	3.5	3.4	3.4	4.5	3.2
5-10	37	3.9	4.0	4.0	3.7	3.6	3.8	4.2	3.7
10-30	89	3.8	3.8	3.8	3.5	3.5	4.1	4.3	3.6
30-100	78	3.9	3.6	3.8	3.3	4.1	4.0	4.7	3.6
>100	48	3.8	4.1	3.6	3.2	3.9	3.8	4.4	3.9
<b>Total</b>		<b>3.8</b>	<b>3.8</b>	<b>3.8</b>	<b>3.5</b>	<b>3.7</b>	<b>3.9</b>	<b>4.4</b>	<b>3.6</b>

Source: CPP Benchmarks; MFI data (institution type, assets) from MIX Market.

\* Privacy of Data, with lowest number of data sources (3), should not be compared with other categories.

Tan = lowest-scoring region; blue = highest-scoring region; n/a = fewer than five MFIs evaluated.

## Appendix VII. “Getting Started Questionnaire”

The list of questions below each client protection principle reviews the main issues that should guide the implementation of that principle. Questions highlighted in green reflect areas of key importance.

The list is based on the earlier, pre-June 2011 version of the principles. Some differences will be noted, include the absence of the new principle, Appropriate Products Design.

**1: Preventing over-indebtedness:** A financial institution measures up to this principle by carefully establishing the borrower’s ability to afford the loan and repay it. Borrowers should be able to handle debt service payments without sacrificing their basic quality of life.

<b>Monitoring borrower over-indebtedness</b>	1. Management regularly monitors levels of borrower over-indebtedness and uses that information to improve products, policies and procedures.
<b>Suitable products</b>	2. The financial institution offers multiple or flexible loan products that address different business and family needs.
<b>Repayment capacity evaluation</b>	3. The loan approval process requires evaluation of borrower repayment capacity & loan affordability. Loan approval does not rely solely on guarantees (whether peer guarantees, co-signers or collateral) as a substitute for good capacity analysis.
<b>Debt thresholds guidelines</b>	4. Credit approval policies give explicitly address borrower debt thresholds and acceptable levels of debt from other sources.
<b>Credit history verification</b>	5. When available, the financial institution checks a Credit Registry or Credit Bureau for borrower current debt levels and repayment history. When not available, the financial institution maintains and checks internal records and consults with competitors for same.
<b>Portfolio quality valued</b>	6. Productivity targets and incentive systems value portfolio quality as much as other factors, such as disbursement or customer growth. Growth is rewarded only if portfolio quality is high.
<b>Internal audit monitoring</b>	7. Internal audits check household debt levels, lending practices that violate procedures (such as unauthorized re-financing and multiple borrowers or co-signers per household) and other practices that could increase indebtedness.

**2a: Transparency:** A financial institution measures up to this principle by ensuring that complete information is made available to customers in clear language that is not misleading and that the customer is able to understand.

<b>Disclosure of prices, terms &amp; conditions</b>	1. Prices, terms and conditions of all financial products are fully disclosed to the customer prior to sale, including interest charges, insurance premiums, minimum balances , all fees, penalties, linked products, 3rd party fees, and whether those can change over time.
<b>Staff training</b>	2. Staff is trained to communicate effectively with all customers, ensuring that they understand the product, the terms of the contract, their rights and obligations. Communications techniques address literacy limitations (e.g., reading contracts out loud, materials in local languages).
<b>Variety of disclosure mechanisms</b>	3. The financial institution uses multiple channels for disclosing clear and accurate information about the product, such as brochures, orientation sessions, meetings, posting information in the branch, websites, etc.

<b>Total cost disclosure</b>	4. The financial institution follows truth-in-lending laws and required APR or effective interest rate calculation formulae. In the absence of industry-wide requirements, the institution provides information that shows the total amount that the customer pays for the product.
<b>Loan contract &amp; collection practices disclosures</b>	5. Loan contracts (1) show an amortization schedule that separates principal, interest, fees; (2) define the amount, number and due dates of installment payments; and (3) include fees and conditions for early repayment, late payments and default. Debt collections practices are revealed to the borrower prior to the time of sale.
<b>Adequate time for client review</b>	6. Customers are given adequate time to review the terms and conditions of the product and have an opportunity to ask questions and receive information prior to signing contracts.
<b>Accurate and timely account information</b>	7. Customers regularly receive clear and accurate information regarding their accounts (e.g., account statements, receipts, balance inquiries).

**2b: Responsible Pricing.** A financial institution can measure up to this principle by offering quality services for the price, demonstrating its competitiveness in the marketplace, and favoring a long-term beneficial relationship with the customer over short-term profit maximization. Consistent practice of transparent pricing is a pre-condition to adequate implementation of this principle.

<b>Competitive, unsubsidized pricing</b>	1. Prices are not subsidized, are market oriented and competitive within the country context.
<b>Prices do not reflect inefficiency</b>	2. The financial institution does not charge customers for its own inefficiency, as demonstrated by a comparison of efficiency and profitability ratios of similar competitors.
<b>Reasonable rate of return</b>	3. The institution earns a reasonable rate of return to support operations and grow, while allowing the customer to do the same.
<b>Re-investment of profit benefits client</b>	4. The financial institution invests a portion of its profits to increase value to customers, such as lowering interest rates or adding or improving products and services.
<b>No excessive penalties or fees</b>	5. Pre-payment penalties or account closure fees and other penalties are not excessive. For example, they would not prevent a customer from changing to another product or provider, or unreasonably compound debt.

**3: Appropriate Collections Practices:** A financial institution measures up to this principle by treating customers with dignity even when they fail to meet their contractual commitments.

<b>Practices written in manual</b>	1. Acceptable and unacceptable debt collection practices are clearly defined in a code of ethics, staff rules or debt collection manual.
<b>Staff and 3rd party training</b>	2. Collections staff receive training in acceptable debt collections practices and procedures. In-house and, if applicable, 3rd party collections staff are expected to follow the same practices.
<b>Non-compliance disclosure and sanctions</b>	3. Staff is informed in advance of penalties for non-compliance with collections policies and violations are sanctioned.
<b>Acceptable collateral policies</b>	4. The institution uses a policy on acceptable pledges of collateral, including not accepting collateral that will deprive borrowers of their basic survival capacity.
<b>Rescheduling policies and procedures</b>	5. Re-scheduling policies prevent automatic debt extensions and re-scheduling procedures follow written protocol.

**4: Ethical Staff Behavior:** A financial institution measures up to this principle by creating a corporate culture that values high ethical standards among staff and ensuring safeguards are in place to prevent, detect and correct corruption or customer mistreatment.

<b>Valued &amp; rewarded</b>	1. The institution's corporate culture values and rewards high standards of ethical behavior and customer service.
<b>Expressed in the code of ethics</b>	2. A written code of business ethics defines organizational values and the standards of professional conduct expected of all staff.
<b>Board approval and staff compliance</b>	3. The code of ethics has been reviewed and approved by the Board and is included in staff rule book or administrative policies.
<b>Acceptable/Non-acceptable behavior &amp; reprimands</b>	4. Staff rules include specific provisions on what is considered acceptable and unacceptable behavior. Provisions describe reprimands and actions that can result in termination of employment.
<b>Alignment of HR practices</b>	5. HR procedures pay attention to ethics, such as assessing new employees for compatibility with organizational values.
<b>Staff training</b>	6. Staff receives orientation and refresher courses on the practicalities of following codes of conduct.
<b>Performance evaluations review ethics</b>	7. Managers and supervisors review ethical behavior, professional conduct and the quality of interaction with customers as part of staff performance evaluations.
<b>Detection systems for client mistreatment</b>	8. The institution has a robust internal audit and fraud control system that detects customer mistreatment, such as soliciting kickbacks and favors or using coercion.

**5: Mechanisms for Redress of Grievances:** A financial institution measures up to this principle by having a mechanism for collecting, responding in a timely manner, and resolving problems for customers.

<b>Written complaint policy</b>	1. A written policy requires customer complaints to be taken seriously, fully investigated and resolved in a timely manner without bias.
<b>Active handling process</b>	2. A mechanism to handle customer complaints is in place, has dedicated staff resources, and is actively used. (Suggestion boxes alone are generally not adequate.)
<b>Resolution monitoring system</b>	3. Customers are informed of their right to complain and know how to submit a complaint to the appropriate person.
<b>Staff training</b>	4. Staff is trained to handle complaints and refer them to the appropriate person for investigation and resolution.
<b>Resolution &amp; progress monitoring system</b>	5. Internal audit or other monitoring systems check that complaints are resolved satisfactorily.
<b>Incorporation of feedback</b>	6. Complaints information is used to improve products, sales techniques and other interactions with customers.

**6: Privacy of client data:** A financial institution measures up to this principle by respecting the privacy of customer data, ensuring the integrity and security of their information, and seeking their permission to share information with outside parties prior to doing so.

<b>Written privacy policy</b>	1. A written privacy policy governs the gathering, processing, use and distribution of client information.
<b>Secure systems and staff training</b>	2. Systems, including secure IT systems, are in place and staff trained to protect the confidentiality, security, accuracy and integrity of customers' personal and financial information.

<b>Client understanding and consent</b>	3. Customers know how their information will be used. Staff explains how data will be used and seeks permission for use.
<b>Written consent required</b>	4. Written customer consent is required for use of information in promotions, marketing material and other public information. Customers are asked to express their written agreement for sharing personal information with any external audience, including credit bureaus.
<b>Client education</b>	5. The institution offers information, orientation or educational sessions to clients on how to safeguard information, access codes or PIN numbers.

*Cover Photograph*

Photographer Credit: John Rae for ACCION International.

Caption: Loan officers visit market in Ghana, 2008.



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